NEIGHBORHOODS: THE BLAMELESS VICTIMS OF THE SUBPRIME MORTGAGE CRISIS

HEARING

BEFORE THE

SUBCOMMITTEE ON DOMESTIC POLICY

OF THE

COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM

HOUSE OF REPRESENTATIVES

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NEIGHBORHOODS: THE BLAMELESS VICTIMS OF THE SUBPRIME MORTGAGE CRISIS

WEDNESDAY, MAY 21, 2008

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON DOMESTIC POLICY,
COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM,
Washington, DC.

The subcommittee met, pursuant to notice, at 2:10 p.m., in room 2154, Rayburn House Office Building, Hon. Dennis J. Kucinich (chairman of the subcommittee) presiding.

Present: Representatives Kucinich, Cummings, Watson, Tierney, and Higgins.

Also present: Representative Turner.

Staff present: Jaron R. Bourke, staff director; Jean Gosa, clerk; Charisma Williams, staff assistant; Leneal Scott, information systems manager; Janice Spector, minority senior professional staff member; John Cuaderes, minority senior investigator and policy advisor; and Benjamin Chance, minority professional staff member.

Mr. KUCINICH. Good afternoon. The Subcommittee on Domestic Policy of the Committee on Oversight and Government Reform will now come to order.

Today's hearing will explore the cost to neighborhoods caused by concentrations of vacant and abandoned houses, differences between strong housing markets and weaker ones, strategies to mitigate the effects of and prevent vacancies, and estimates of the size of the national problem.

Without objection, the Chair and ranking minority member will have 5 minutes to make opening statements, followed by opening statements not to exceed 3 minutes by any other Member who seeks recognition.

And, without objection, Members and witnesses may have 5 legislative days to submit a written statement or extraneous materials for the record.

I would like to remind everyone that, under a previous unanimous consent agreement, Mr. Turner of Ohio is allowed to sit as a member of the subcommittee on issues related to State and local governments. As the former mayor of Dayton, Ohio, we welcome him to these proceedings. And, of course, the issue we're exploring today falls under the categories previously described. As chairman of the Federalism Subcommittee in the previous Congress, he has great knowledge on these issues.

And I want to say that we welcome his presence here today, as do I welcome the presence of my colleague from California, Ambassador Watson. Thank you very much for being here.

And I would like to thank everyone for their attendance.

The Domestic Policy Subcommittee of the Oversight and Government Reform Committee has held three hearings on the effects of foreclosures since 2007. These include a 6-hour, 15-witness marathon hearing in March 2007, as well as a field hearing in Cleveland, Ohio, one of the most foreclosure devastated areas in the country.

While awareness has grown that the meltdown of subprime lending has been a genuine tragedy for millions of individual borrowers and lenders, today's and tomorrow's hearings are about a largely unrecognized, deeply suffering and totally blameless victim: neighborhoods.

Some foreclosed properties find new buyers; many do not. When foreclosure leads to vacant and abandoned houses, surrounding neighborhoods and local municipalities suffer significant consequences.

Those effects include: falling property values of surrounding houses; loss of equity held by neighbors in these houses; loss of rental units for renters; loss of sales to neighborhood merchants; increasing crime; rise in municipal costs in police, fire due to vandalism and arson; increased demolition and building inspection costs; increased legal expenses; increased demand on city social service programs; and a direct loss of property tax revenues.

Economic researchers have found that the police costs for responding to criminal activity alone in vacant and abandoned houses adds up to between $5,000 and $6,000 per property. With demolition costs, the municipal cost per vacant property rises to $19,227. If the property is subject to arson, the cost rises to $34,199.

The collective cost to neighbors within a 150-foot radius of a block in Chicago with a large concentration of vacant properties amounted to $220,000 in terms of capital depreciation of their own properties. To our knowledge, there's no comprehensive cost estimate for the Nation, but it would surely have to be in the many billions.

There are significant costs borne by people who had nothing to do with the transactions that resulted in the subprime mortgage meltdown. They weren't the lenders, they weren't the investors, they weren't the borrowers. They were simply the neighbors, renters and taxpayers.

This Congress has taken a significant step to help the neighbors deal with the problem they're now facing. Two weeks ago, the House passed H.R. 5818, the "Neighborhood Stabilization Act of 2008." This bill creates a new Federal program to address the effects on neighborhoods caused by the foreclosure crisis. The bill authorizes $15 billion in grants and loans to be spent by localities on a variety of strategies, including vacant-property acquisition, building rehabilitation and demolition.

The House agreed to an amendment, which I had offered, clarifying that the purpose of the bill is to address the consequences for neighborhoods of a rise in the level of vacant and abandoned buildings, and requiring local governments to target their spending accordingly. Unfortunately, the President issued a veto threat. I really can't understand this, but I hope that today and tomorrow's

hearing might do something to change his mind. For if we can't help the totally innocent, the neighbors of these vacant properties—and they are the innocent victims of the foreclosure crisis—then who should we help?

Now, fortunately, we have some of the Nation's leading experts with us today and tomorrow to help explain the problem neighborhoods face and help guide a Federal response.

When I speak of these issues, when I hear the witnesses, I just want to add a personal note here, I started my career in the city of Cleveland over 41 years ago. I started at the local level, at the community level. I served on the Cleveland City Council many terms, and I served the city as mayor. I realize at a local level the kind of impact that this foreclosure crisis is having.

When I was a Councilman, if there was a single house in the ward that was abandoned, vacant or boarded up, it was a cause to the whole community. Today, in some communities, there are hundreds and maybe even over a thousand.

Just imagine you're a senior citizen who has taken care of your property for your whole life, and the neighborhood around you starts to change economically but you still take care of your property. And then you get into the subprime situation. We have all these vacant properties all of a sudden. The equity that you had is your retirement security, and it's disappearing.

This is a very serious matter that merits the attention of the Congress, which is why we're having this hearing now. But also it's good to know that we have Members of the House who are going to be involved in this, not just from Ohio and California, but from New York, the Buffalo area, with my colleague that has just joined us, Congressman Higgins.

So does the gentleman from Ohio, do you have an opening statement?

Mr. TURNER. Well, thank you——

Mr. KUCINICH. I recognize Mr. Turner from Ohio.

Mr. TURNER. Thank you, Chairman Kucinich.

I appreciate you holding this hearing and you allowing me to participate. It's great to have two former Ohio mayors come together to look at the issue of what's happening in our neighborhoods in Ohio. Unfortunately, it is a very negative picture. But I appreciate what you're doing to highlight this issue and to look at solutions and what we can do.

The home foreclosure crisis once associated with just Ohio and Michigan is now being felt across the rest of the country and is also rattling our international markets. As these hearings hopefully will demonstrate, problems associated with home foreclosures are felt by more than just the people whose homes are foreclosed.

For the most part, individual foreclosures in and unto themselves are not a community-wide issue. It becomes an issue when a community faces multiple home foreclosures in a concentrated area. Under this scenario, the problem, if left untreated, can turn once-thriving neighborhoods into an area of blight. Statistics show that this problem is encompassing both our inner-city neighborhoods and suburban neighborhoods alike.

Fixing this problem will be easy. Although increased home foreclosures are a national problem, a one-size-fits-all solution is not

the answer. Addressing the foreclosure problem in Ohio will require a different solution than how we treat the same problem in perhaps another State. If we are truly to assist in resolving the foreclosure problem, then a Federal solution must be well thought out with a formula that recognizes that affected areas need more help, some than others.

Many communities faced with high foreclosure rates will have an easier time recovering. Foreclosures in areas where real estate is considered highly marketable will need very little Federal assistance. On the contrary, those with multiple foreclosures and difficulty in resale will see that the process of foreclosure frequently leads to abandonment.

Mr. Chairman, I appreciate your efforts to highlight these problems associated with home foreclosures. I look forward to working with you.

And I have to give one acknowledgement from my community, as we go forward with this. When I served as mayor for the city of Dayton, Commissioner Dean Lovelace on our commission brought forth the issue of predatory lending and sounded the alarm in our neighborhood of what was happening to families that were being subject to foreclosure, with the prediction of what would happen in our neighborhoods and, ultimately, the prediction of what would happen nationwide and, as we've seen, failings in our financial markets.

In July 2001, he pushed forward a predatory lending ordinance which was intended to assist our community. In both Ohio as a State and on the Federal level, we were very slow to act, and I think this is a real reason why we need to step forward in the many areas to provide assistance to both homeowners and to neighborhoods to try to address some of the impacts of foreclosure and abandonment.

And, Mr. Chairman, I just thank you for bringing this forward and highlighting it so we can look at solutions and our real impacts on our neighborhoods. Thank you.

Mr. KUCINICH. I thank the gentleman. It's a pleasure to work with him on this.

The Chair recognizes the gentlelady from California, Congresswoman Diane Watson.

Ms. WATSON. Thank you, Mr. Chairman. And thank you for holding today's very important hearing about the subprime mortgage crisis.

The mortgage crisis affecting our Nation is one of the most pressing domestic issues of the new millennium. In California, my home State, the number of homes that were lost to foreclosure during the first quarter of 2008 surged 327 percent from 2007 levels. In the terms of numbers, it means that there were 517 foreclosures every day for 3 months.

If more is not done to restrain the trend of rising foreclosures, I believe Congress will find that neighborhoods would have significant increases in vacated or abandoned houses; neighborhoods would lose value; local governments would be overwhelmed with having to deal with increases in crime; social service programs would be in greater demand, which requires municipalities to spend more; and losses in tax revenue from a declining property-

tax base would help lead to the decline in government infrastructure projects, such as schools, roads and public safety.

Once the second quarter is finished and it is determined if the economy is in recession or not, Congress should determine immediately if the problem with the rise in foreclosures is limited to the subprime market or has the problem spilled into the mainstream home loan market.

Hopefully, that will not be the case. But if it is, we will find that more and more neighborhoods would be affected by a concentration of abandoned and vacant houses, which is not in the best interest of our local communities or our Nation as a whole.

I look forward to hearing the testimony, Mr. Chairman, of our panelists today and working with my colleagues to help our Nation recover from the foreclosure crisis.

Thank you, and I yield back the remainder of my time.

Mr. KUCINICH. I thank the gentlelady.

The Chair recognizes the distinguished representative from the Buffalo area, Congressman Higgins.

Mr. HIGGINS. Thank you very much, Mr. Chairman.

And I, like you, in representing the city of Cleveland and the city council, I represented the city of Buffalo in the city council as well. And much like a lot of areas of the urban Northeast, these areas were great economic centers through most of the 20th century and, over the past 30 years, have declined significantly, losing population not only to other areas of the country but also to the surrounding suburban areas.

The urban cores of these cities were once great. They can be great again. But what fundamentally has to be addressed is the issue of vacant and abandoned housing.

In the city of Buffalo, it's a problem that's pervasive and growing. This administration has withdrawn from its commitment to help urban areas and has an obligation to retool its efforts to ensure that cities like Cleveland, cities like Buffalo and the great urban centers of the American Northeast are restored. And that starts and ends with a healthy, strong urban environment. Fundamental to that is the housing stock.

So I look forward to working with you, Mr. Chairman, on this issue, and I applaud your leadership in that regard.

Mr. KUCINICH. I thank the gentleman.

I would ask the witnesses to come forward, Mr. Kildee and Ms. Floreen.

While you're taking your seats, I would like to let the Members know and those who are in our audience know who is about to be testifying.

Mr. Daniel Kildee is the treasurer of Genesee County in Michigan. Mr. Kildee initiated the use of Michigan's new tax foreclosure law as a tool for community development in neighborhood stabilization. He founded the Genesee Land Bank—that was Michigan's first land bank—and now serves as its chairman and chief executive officer. Mr. Kildee is also president of the Genesee Institute, a research and training program focusing on urban land reform, smart growth and land banking.

And for those of you who are familiar with the name Kildee, yes, according to the information we have, Mr. Kildee is the nephew of

Congressman Dale Kildee, who is one of the highly respected Members of our U.S. Congress.

We welcome you, Mr. Kildee.

The next witness will be Ms. Nancy Floreen. Ms. Floreen is testifying on behalf of the National Association of Counties, the U.S. Conference of Mayors, the National Community Development Association, and the National Association of Local Housing Finance Agencies.

Ms. Floreen is a county council member in Montgomery County, MD. She serves as a member of the council's Planning, Housing and Economic Development Committee. Previously, she has served as the commissioner of the Maryland National Capital Park and Planning Commission. She's a member of the Montgomery County Planning Board and a member of the Maryland Citizen Planners Association.

I want our witnesses to know, Mr. Kildee and Ms. Floreen, that it is a policy of the Committee on Oversight and Government Reform to swear in all witnesses before they testify.

I would ask that you rise and raise your right hands.

[Witnesses sworn.]

Mr. KUCINICH. Thank you very much.

Let the record reflect that each witness answered in the affirmative.

I would ask that each of the witnesses now give a brief summary of your testimony. Keep the summary under 5 minutes in duration. Keep in mind that your entire statement will be in the record of this hearing and will be available to all the Members, not only of this committee but of Congress.

Mr. Kildee, you are going to be our first witness. I want to thank you, and I would ask that you proceed with your statement.

STATEMENTS OF DANIEL T. KILDEE, TREASURER, GENESEE COUNTY, MI; AND NANCY FLOREEN, COUNCILMEMBER, MONTGOMERY COUNTY, MD

STATEMENT OF DANIEL T. KILDEE

Mr. KILDEE. Thank you, Mr. Chairman.

And thank you for your leadership on this issue. You and other members of the committee obviously have helped to bring this entire issue to the national stage. And for those of us that are working in places like Flint and Dayton and Buffalo and other communities across the country that have experienced significant population loss and decline, we appreciate it.

In fact, many of us have been working on this issue for quite some time. It's only recently that this mortgage crisis has brought the issue of vacant and abandoned properties to a higher level of consciousness. So it's, first of all, my hope that the current conversation taking place surrounding the mortgage crisis will lead to more fundamental reforms that place a higher value on the urban landscape generally.

I'm from Flint, Michigan and, as the chairman said, the home of myself and my Congressman, Dale Kildee. Flint is the birthplace of General Motors. We once had 79,000 people working for the same company in our city. We had a population in 1960 of 197,000.

Today it's about 115,000 people. And so, while we have a lot of anxiety about the 5,000 or 6,000 mortgage foreclosures that are pending in our own community right now, we've been dealing with vacant and abandoned property for quite some time.

When we lost 40 percent of our population over 30 years, those people who left did not take their houses with them. And they left behind a landscape that has seriously deteriorated.

The cost of that abandonment is what concerns us. Seventy percent of the fires that take place in Flint, Michigan, take place in an abandoned house. So our fire department in the city of Flint has to be three or four times what it would be if that fuel were not out there in the neighborhoods.

This year, we have seen an increase in tax delinquency. All of this mortgage meltdown is resulting in higher rates of tax delinquency as well. Two years ago, I had $29 million of delinquent taxes in the county. Last year, it was $37 million of delinquent taxes. And, this year, there are $49 million in unpaid taxes in Genesee County. All of it being exacerbated by the fact that literally thousands of properties held by lenders or servicers are not paying their taxes.

In my community, about 5 or 6 years ago, we began the process of getting our arms around this problem by creating a land bank authority and reforming our tax foreclosure procedures.

We eliminated the somewhat antiquated procedure of selling tax liens to private investors, because we saw with tax foreclosure how negative the liquidation model had become for the urban landscape. That old tax lien system is a lot like how mortgage lenders are now disposing of mortgage-foreclosed assets.

We reformed our process. We now, as the county treasurer, get control of these properties and dispose of them in a way, through our land bank authority, that considers the long-term interests of the neighborhoods, of the urban landscape, of the private equity that's already in place.

Our fear, of course, is that, while we have made great progress in Flint in getting our arms around the problems associated with that first wave of abandonment—for example, we've taken title to 7,400 properties in the last 6 years into our land bank authority, 12 percent of the parcels of land in the city of Flint. Our fear is that, while we've done all this work to reform our State and local systems to deal with abandonment, this next wave of property is sitting out there, heading our way.

The cost is enormous. The cost to local government, with the reduction of the tax base and the uncollected taxes that we're unable to use to provide basic services, occurs at the same time that the conditions in these neighborhoods increase the demand for government services. Our water and sewer systems are built for a population of 250,000. We've got 150,000 users paying to maintain that system. The stress on local government is enormous.

And the loss of private equity, those homeowners in those neighborhoods, as the chairman said, who pay their mortgage, they pay their taxes, and they're having the equity that they've invested in that home robbed from them for something that they, quite honestly, had nothing to do with.

This is a problem—interesting now that places like Flint and Dayton and Buffalo and others, Cleveland for sure, that have been associated with the problem of vacant and abandoned property historically, this is a problem now being experienced in all sorts of cities.

The concern that I have as the Federal response is being developed is that there be some recognition that the older—particularly older, industrial—cities that have been dealing with abandonment for quite some time do not have the strength in the real estate market to absorb, in our case, 5,000, 6,000, 7,000 new abandonments.

I mean, every community that's dealing with mortgage foreclosures obviously are going to have a difficult time. The problems in a place like Flint, where we already have an oversupply in a very weak demand market of a low-value housing commodity, the problems associated with 5,000 new abandonments or 5,000 distressed sales coming into our marketplace are frightening.

What we have to avoid, I think, in our community and as a Nation is a situation that could lead to mortgage lenders and servicers essentially privatizing the profit by liquidating the properties that have value and socializing the loss by passing them on to us.

I just foreclosed on March 31st, through the tax foreclosure system, on 1,194 properties. Over 300 of them had mortgages on them, and they're upside down in value. Those lenders have passed that problem on to us. We're willing to accept it, but we would like to accept it with the ability to also go to those same servicers and lenders and say, "You know, there are other assets that you own in our community, and we would like to talk to you about them as well."

This a problem that, obviously, I care deeply about. It's a problem that's affecting Flint, Michigan, in my own neighborhood. And it's one that I look forward to providing you assistance with as you deliberate on this very important subject.

Thank you.

[The prepared statement of Mr. Kildee follows:]

Testimony
of
Daniel T. Kildee
Genesee County Treasurer
Wednesday, May 21, 2008
2154 Rayburn HOB
2:00 p.m..
Domestic Policy Subcommittee
Oversight and Government Reform Committee

For decades, cities across the nation have struggled with the daunting problem of abandoned houses and vacant land. Particularly in Michigan, where the cities of Detroit, Flint, Saginaw, and others have experienced significant population loss, the problem has been exacerbated by the absence of a coherent governmental approach to urban land reform.

For the most part, this legacy of abandonment is the result of years of decline associated with the migration of population from the city to suburban communities. Recently, however, the abandonment of the urban landscape has been magnified by the dramatic increase in mortgage-foreclosed homes flooding this already weakened real estate market. While this problem is already having an impact on my community, the fact that there are between 5,000 and 6,000 mortgage foreclosures pending in my community is a matter of great concern, particularly in light of the weak real estate market in Flint and the presence of thousands of previously abandoned homes already littering once thriving neighborhoods.

Abandoned property is a source of blight, crime, and disease. Vacant urban land reduces the very resource available to address the problems it creates. Local property taxes are made less available due to devaluation of land values. For example, abandoned houses account for 75 to 90 percent of fires in the City of Flint, yet the City has reduced fire service due to a significant financial crisis. Given the enormous financial pressure for basic city services, it is clear that reform of urban land is fundamental to revitalization of our cities.

Vacant land is both a cause and result of urban disinvestment. As cities have experienced population loss and housing market declines, the result is the decline of property values. Blight spreads as empty houses sit vacant, infecting adjacent properties and ruining entire neighborhoods in a matter of just a few years. An abandoned house is a "Typhoid Mary" to a neighborhood struggling to sustain itself.

Sadly, for the past several decades, one of the governmental systems intended to address the problem actually contributed to the downward spiral of land values and neighborhood stability. Under the former system of tax foreclosure, abandoned properties were either transferred to private speculators through tax lien sales or became state-owned property through foreclosure. Under either scenario, local leaders had little power to interrupt the

incremental decline in the reutilization of tax-reverted land. In fact, the former system encouraged low-end reuse of tax reverted land due to the length of time between abandonment and reuse – often more than five years. The lack of clear title to these properties under the tax lien system also made reinvestment almost impossible.

The former system was decidedly non-strategic

The changes to Michigan's tax foreclosure law are a significant step in the right direction. Since the passage of PA 123 of 1999, the State of Michigan and county governments have greater authority in gaining control of vacant abandoned land. PA 123 of 1999 accelerated the process of tax foreclosure, which previously took as long as seven years to complete. The new system of county or state tax foreclosure is completed within a two-year period, and abandoned property is taken after only one year.

While the new system is significantly more efficient, we need to go further in order to optimize the reuse of vacant urban land with long-term neighborhood stability in mind. Michigan needs a systemic approach to urban land that affords local government the tools necessary to manage the "downsizing" of cities more effectively. It is only through smart "downsizing" that cities can ultimately seek to grow again.

For communities with significant numbers of abandoned property, a land reutilization plan that delivers tax-foreclosed property to its best and highest use is needed.

Faster and more efficient demolition of existing structures is the earliest and most tangible benefit of such a system. Over time however, land assembly for development and long and short-term green space development is made possible by "land banking" tax reverted property, rather that simply selling land at public auction. Replacing one irresponsible landlord with another is no solution to the problems of sub-standard housing and neighborhood blight. Quickly auctioning tax-reverted property, while somewhat more desirable than the former system, does not provide urban communities the control of land essential to a coherent revitalization plan. Encouraging and supporting locally derived land reutilization planning is essential to urban land reform.

Adoption of legislation that authorizes a foreclosing county to create a "land bank" is one key step in any comprehensive urban land reform initiative. Such legislation was introduced in the previous session of the legislature. While there may be some changes needed to the previously introduced legislation, a land bank is an important component of Genesee County's vision for revitalization of our urban center.

Another policy initiative receiving serious state government attention involves the "smart growth" concept, a popular phrase in current land use lexicon. A commitment to including urban land reform issues as a central subject of the "smart growth" discussion is essential to the development of meaningful policy.

To fully realize the goal of preserving farmland, open green space, and undeveloped land for future generations, we must unlock the unrealized value that urban land presents.

Such reform will benefit cities, suburbs, and rural communities as well. As we struggle to address two serious challenges – maintaining our precious natural resources and preserving and revitalizing our urban centers, we must create public policy which ensures urban land is not overlooked. Such an approach will allow us to support our cities and at the same time preserve the precious resources that have made Michigan such a beautiful place to live.

In Flint, we have made tremendous progress in just a few years by re-engineering the tax foreclosure system. The overriding philosophy of our initiative is that the land itself has value that is far more important than the liquidated value of the property sold at a distressed sale.

If there is not a similar approach to the disposition of mortgage-foreclosed properties, all the good work being done around the state of Michigan in reforming the tax foreclosure system will be overwhelmed with speculative purchasers mismanaging the real estate within our communities and driving down home prices – robbing responsible homeowners of their hard-earned equity.

The remainder of my written testimony is a description of the work of the Genesee County Land Bank. I submit this report to provide additional background on our work and its potential application in restoring the urban landscape, and in particular to explain how a locally controlled land bank authority may be a viable mechanism for disposition of mortgage-foreclosed properties.

Thank you for the opportunity to provide my thoughts to you and the committee as you deliberate this important and growing issue facing the nation.

Mr. KUCINICH. I thank the gentleman for his very fluid and comprehensive statement about the underlying economic crisis that is occurring in urban communities and in cities and, of course, in your own county of Genesee, with respect to the concomitant effects of the subprime mortgage fiasco.

I look forward to the testimony of the next witness, Ms. Floreen.

I would ask that you proceed, and please keep your statement to 5 minutes or less. Thank you.

STATEMENT OF NANCY FLOREEN

Ms. FLOREEN. Thank you, Mr. Chairman.

Mr. Chairman and members of the subcommittee, thank you very much for the opportunity to appear before you today to address the impact of the mortgage crisis on neighborhoods.

It's a special honor for me to be with former local elected officials who have been elevated to this position, because, as you know, at the local level, that is where the rubber hits the road.

Local officials across the country are pleased that the House of Representatives recently passed the Neighborhood Stabilization Act of 2008, providing $15 billion in urgently needed loans and grants to help cities, urban counties and States deal with the foreclosure crisis that's overtaking the Nation. This really does recognize the severity of the problem nationally.

Cities and counties will be able to use this funding for the purchase and rehab of vacant and foreclosed homes. It would help stabilize communities by reselling the homes for occupancy as soon as possible. We really need this legislation to address the crisis.

You've heard from Mr. Kildee, certainly the chairman's comments at the beginning. There's very little to add. But across the United States, this problem threatens billions of Federal dollars invested in neighborhood revitalization over the years. It is a fact that foreclosed homes drive down the value of surrounding problems. And the sooner that we solve this problem, the less collateral damage we'll have with depreciating home values.

This cuts directly to what's the mainstay of local government revenues: property taxes. We cannot adequately fund schools and other essential public services if we have a prolonged decline in property values. Some estimates put the number of foreclosed properties at 600,000 or more, and the problem is simply too great for counties and cities to tackle on their own due to their own declining tax bases.

Even in Montgomery County, Maryland, right up the road, we've not been immune to the housing crisis. Notice of foreclosure sales in my county have increased from 68 during the first quarter of 2007 to 918 during the first quarter of 2008, an increase of 1,250 percent—nothing like Mr. Kildee's numbers, but nonetheless for us this is huge.

A total of 611 notices of mortgage loan default were issued in the first quarter, compared with 103 in the first quarter of 2007, an increase of nearly 500 percent.

We're trying to deal with this by participating in the Maryland HOPE Hotline for residents facing foreclosure. We've been offering homeownership and foreclosure solution sessions across the county. We've partnered with the State to provide assistance to residents,

and contributing money to nonprofits to provide counseling to homeowners.

But we're also using our own money on matching State contribution to develop a credit enhancement program to encourage local banks to refinance loans for individuals subject to foreclosure who might require special underwriting criteria.

But like many local areas across the country, we're grappling with budget shortfalls. When a local government is faced with declining revenues, it's basically two choices: increase tax rates or make cuts in services.

As many of your staff will tell you, Montgomery County is looking at the increasing-the-taxes approach right now. And I'm very concerned about how much farther we can go to provide the services our residents need and deserve.

The neighborhoods are, indeed, innocent bystanders in the subprime mortgage chaos. It will take more than a local or State remedy to curb the decline. The funding provided by H.R. 5818 is timely, targeted and temporary.

We'll work closely with members of the conference committee as they reconcile the House and Senate bills.

The Senate version provides an emergency appropriation of $4 billion in Community Development Block Grant funds to be allocated based on a formula to be developed within 60 days of enactment. We'll be urging the conferrees to, one, utilize the CDBG program as the program to deliver assistance, as in the Senate bill, with 70 percent of the funds to entitlement cities in urban counties. CDBG grantees are intimately familiar with that program. The funds made available under the bill are for the very types of activities that they carry out on a regular basis.

No. 2, we'll work with you to provide that funding for foreclosure relief and mitigate be in the form of grants for ease of administration.

Three, we'll work with you to permit the funds to be used to assist families with earnings up to 140 percent of median income, with 25 percent of the funds to be used by households at 50 percent of median.

We'll work with you to permit 5 percent of the funds to be used for administrative costs. This is consistent with CDBG funding made available to respond to Hurricanes Katrina and Rita.

Thank you very much for your favorable consideration of our views.

[The prepared statement of Ms. Floreen follows:]

Statement of the Honorable Nancy Floreen
Councilmember, Montgomery County, Maryland
National Association of Counties

Before the United States House of Representatives
Committee on Oversight and Government Reform

Domestic Policy Subcommittee

On behalf of the
National Association of Counties
United States Conference of Mayors
National Association of Local Housing Finance Agencies
National Community Development Association

Impact of Mortgage Crisis on Neighborhoods

May 21, 2008

Chairman Kucinich, Ranking Member Issa and members of the subcommittee, thank you for the opportunity to appear before you today to address the Impact of the Mortgage Crisis on Neighborhoods. My name is Nancy Floreen; I am a County Councilmember from Montgomery County, MD and a member of the National Association of Counties. I have been a Montgomery County At-Large Councilmember since 2002 and I am also a former Mayor of the town of Garrett Park, MD. Today, I have the privilege of representing the National Association of Counties (NACo) as well as the U.S. Conference of Mayors, the National Association of Local Housing Finance Agencies and the National Community Development Association.

Local officials across this country are pleased that the House of Representatives recently passed the Neighborhood Stabilization Act of 2008, HR 5818. This legislation would provide $15 billion in urgently needed loans and grants to help cities, urban counties and states deal with the foreclosure crisis that is overtaking the nation. Cities and counties would be able to utilize this funding for the purchase and rehabilitation of vacant and foreclosed homes. This assistance will help stabilize communities by reselling the homes for occupancy as soon as possible.

This legislation is vitally needed to address the growing mortgage foreclosure crisis across the United States, a situation which threatens the billions of federal dollars invested in neighborhood revitalization over the years. We strongly support the $15 billion authorized under the bill and its administration by the Housing and Urban

Development office that also administers Community Development Block Grant funds. This amount recognizes the severity of the problem nationally.

The foreclosure crisis affects, tragically, not only those who lose their homes, but those families who are near foreclosure homes. It is a proven fact that foreclosed homes drive down the value of surrounding properties. The sooner we solve this problem, the less collateral damage we will have with depreciating home values. Recently, over half of the top 150 metro areas saw a decline in the median sales price of existing single family homes. This cuts directly to what is the mainstay of local government revenues, property taxes. Local governments cannot adequately fund schools and essential public services if we have a prolonged decline in property values.

Foreclosed and abandoned properties are blight on too many neighborhoods across America. Some estimates have put the number of foreclosed properties at 600,000 or more. The problem is simply too large for counties and cities to tackle on their own due to their declining tax bases as a result of the problem. Counties and cities desperately need federal assistance to confront this blight.

Montgomery County, MD has not been immune to the housing crisis. Montgomery County's foreclosure rate continues to worsen. Notice of foreclosure sales in the County increased from 68 during the first quarter of 2007 to 918 during the first quarter of 2008 an increase of 1,250%. A total of 611 notices of mortgage loan default were issued in the first quarter of 2008, compared with 103 notices in the first quarter of 2007, an increase

of 493.2%. As a member of the Planning, Housing and Economic Development Committee in Montgomery County, I have witnessed firsthand the problems facing our residents and neighborhoods and welcome finding solutions.

To assist in lessening the mortgage foreclosure tide, Montgomery County participates in the Maryland H.O.P.E. hotline for residents facing foreclosure or delinquency. Residents can receive free confidential information and counseling 24 hours a day, 7 days a week. We have also been offering homeownership and foreclosure solution sessions across the county. Additional information is available at www.montgomerycountymd.gov .

Montgomery County has officially partnered with the Maryland State Department of Housing and Community Development to provide assistance to residents. The state and county have contributed money to non-profit organizations to provide counseling to homeowners in the county. The Bridge to Hope program provides zero percent interest loans up to $15,000 to households who can use the funds to bridge the time needed to refinance and get their overall financial situation in order. The loan will be repaid upon refinancing. The county is also using $2.5 million from the Housing Initiative Fund (HIF), matching the State's contribution to develop a credit enhancement program to encourage local banks to refinance loans for individuals subject to foreclosure who might require special underwriting criteria.

While counties and cities across this country are taking steps to mitigate the damage from the foreclosure crisis, we cannot do it alone. The federal government has an important

role in assisting counties and cities across this country in saving their neighborhoods. Montgomery County, like many local areas across this country, is grappling with budget shortfalls. When a local government is faced with declining revenues, it has basically two choices: 1) increase tax rates, or 2) make cuts in services due to reduced tax revenues. Residents cannot afford such outcomes and deserve better. Neighborhoods across this country are innocent bystanders in the sub-prime mortgage chaos and it will take more than a local and / or state remedy to curb the decline. This strikes to the competitiveness of our metro economies and by extension, the competitiveness of our national economy. While legally we are a nation of states, economically our nation functions as a group of metro economies. Our 362 metropolitan areas account for over 85 percent of our nation's GDP, employment and labor income. If our metro economies falter, so does the nation. That is why it is imperative that HR 5818 be signed into law as soon as possible to stem the tide and assist neighborhoods and local communities get back on track.

The funding provided by HR 5818 is timely, targeted and temporary. It would enable counties and cities to deal with the foreclosure problem in a straight forward manner by acquiring, rehabbing and reselling these homes. The bill directs the funding to the areas most in need based on a formula that accounts for the number of delinquent (90 days or more) subprime loans. Further, the money must begin to flow within 6 months of enactment, be fully obligated within a year and be fully spent within two years of enactment.

The legislation is a reflection that the foreclosure problem is adversely affecting neighborhoods, often neighborhoods that have already been infused with other federal assistance. That investment is threatened unless action is taken.

We support the legislation's flexibility in the use of funds, i.e. for the Community Development Block Grant-eligible activities, financing mechanisms for redevelopment, purchase and rehabilitation for sale or rental, land banks, demolition, project-based rental assistance and project operating subsidies and reserves. This flexibility will allow communities to address the foreclosure problem as it uniquely affects them.

As the legislation moves toward conference, we urge modification of HR 5818 to allow the funds to flow through the Community Development Block Grant Program (and its allocation of 70% to metropolitan cities and urban counties and 30 percent to the states). This approach is generally embodied in the bipartisan amendment to H.R. 3221, the "Foreclosure Prevention Act of 2008" passed by the Senate. That legislation relies on the Community Development Block Grant (CDBG), a program that Congress nearly always turns to in responding to a disaster, which is applicable to the mortgage foreclosure crisis. Under the Senate legislation, an emergency appropriation of CDBG funding is authorized to be allocated by a formula developed by the Secretary of Housing and Urban Development (HUD). HUD is directed to develop a formula that allocates funding to areas of greatest need based on the number and percentage of home foreclosures in each state or unit of local government, the number and percentage of homes financed by a subprime mortgage related loan in each state and united of local government, and the

number and percentage of homes in default or delinquency in each state or unit of general local government. Grantees are intimately familiar with CDBG, and the funds made available under the bill are for the very types of activities that they carry out on a regular basis. We also believe funding for foreclosure relief and mitigation should be in the form of grants and not so much loans for ease of administration.

We do support the use of funds to purchase or finance the purchase of foreclosed housing for resale to families with incomes up to 140% of median income; to purchase or finance the purchase of foreclosed housing for use by qualified tenants as rental housing; to rehabilitate foreclosed housing; for operating and holding costs; and for administrative costs. We also recommend a 5% administrative allowance *for each grantee* receiving this funding. This 5% allowance is consistent with CDBG funding made available to respond to the devastation caused by Hurricanes Katrina and Rita. Grantees receiving foreclosure relief/mitigation funding will be expected to carryout extensive activities in acquiring and disposing of property. They simply do not have the funds to undertake these activities without an adequate administrative allowance.

Thank you for your favorable consideration of our views.

Mr. KUCINICH. I thank the gentlelady for her testimony.

I would like to begin with asking Treasurer Kildee some questions.

In some ways, you might be the ideal witness to answer this question. Can you tell the committee what lessons may be drawn from Genesee County's experience with both a vacant and abandoned housing problem and a noninterventionist Federal Government?

Mr. KILDEE. The most significant lesson that we learned is that economics really do matter when it comes to urban land. And we cannot allow the governmental systems that are in place to treat property that has significant value with a different set of rules than we treat property that is essentially upside-down in value.

The Genesee County Land Bank and our Michigan Land Bank Act, along with our tax foreclosure reforms, address that issue by not allowing the speculator market to pick and choose and essentially disaggregate the inventory that is the subject of our concern. In our case, initially, it was tax-foreclosed properties. There are valuable properties that get lost through foreclosure. That's why people make those odd infomercials. The idea would be, though, to not allow the lenders to do the very same thing.

Mr. KUCINICH. You have a data base where you can literally see who got into the subprimes, who has come out in the secondary market here, who the speculators are, is that right?

Mr. KILDEE. Right. And the issue, of course, for us is we want to approach, with the support of the Federal Government, with some strength, those lenders and say to them, "Deal with us with your entire inventory. Don't allow the system in place to allow you to essentially liquidate the value that's in those properties for which there may be a speculator market."

Mr. KUCINICH. What kind of Federal aid or Federal assistance or tools would be required by local jurisdiction to strengthen their position vis-a-vis the speculators, the banks that are involved with these subprimes?

Mr. KILDEE. No. 1 would be to have an efficient public entity that can acquire and then manage and dispose the properties. That's critical.

Second would be to target the Federal support and other available support for acquisition of these properties in a fashion that does allow us to approach the lenders with the opportunity, if you want to call it that, for us to acquire their entire inventory within our community.

I think to do this on a regional basis—and that's where I think the counties do play an important role—takes advantage of the more diverse real estate market within the region. And so a city does not have to essentially get stuck with those properties that are underwater in value and not be able to take advantage of whatever retained equity may be out there on those foreclosed assets that are in markets that might be more——

Mr. KUCINICH. By stepping forward the way that you do, do you think that you do a better job than traditionally private sector or real estate tasks—that you can do a better job than what the private sector is doing?

Mr. KILDEE. I think so. But I would say, which private sector? Because there's all sorts of markets for land.

And what I am concerned about is that the for-profit investor market that really will put property into its best and most productive use is the for-profit market that I want to talk to. The problem is the systems that we had in place for tax foreclosure and the worry that I have about mortgage-foreclosed assets is that we're not talking about a system that delivers these properties to that investor market but to the speculative market, to the property flipper.

Mr. KUCINICH. Right. So with the land bank, you have one paradigm. Let's say you don't have a land bank. Can jurisdictions without land banks adequately address significant numbers of vacant properties? How do they do it?

Mr. KILDEE. Well, I think it's up to the capacity of local government or even to the nonprofit sector in a particular community. I'm an advocate of public land bank authorities, because I think it creates the permanent capacity in a single-purpose entity whose job it is to deal with underutilized vacant and abandoned property. It's too easy an issue for somebody to avoid unless you have an entity specifically designed for that purpose.

Mr. KUCINICH. Thank you.

Councilmember Floreen, as you know, Congress passed a bill to help neighborhoods in need. The bill has a veto threat against it. While I would like to be optimistic about the bill's future, will you tell the committee what happens to neighborhoods if the bill is not enacted and if the market alone, the market alone, is relied upon to deal with the growing problem of vacant and abandoned properties?

Ms. FLOREEN. Thank you, Mr. Chairman.

Well, it's very evident that we have left it to the market.

Mr. KUCINICH. That what?

Ms. FLOREEN. We have left it to the market already. And we're seeing the effects of that. There is no question.

Mr. KUCINICH. Could you elaborate?

Ms. FLOREEN. Well, the market that this has been left to is a market that, in many cases, has preyed upon people who cannot afford the situations in which they've been led.

It has particular impact on minority communities. In Maryland, African American homeowners are three times more likely than whites to receive a subprime loan and four times more likely to refinance from a subprime lender. Latinos are twice as likely as whites to receive a subprime loan and three times more likely to refinance from a subprime lender. And those are communities of interest that are particularly hit hard by this.

There is no question that decisions have been made, structures have been created that have led people into a situation which we are collectively faced with having to redefine and solve for the benefit of the communities around those homes.

Mr. KUCINICH. Thank you.

The Chair recognizes Mr. Turner for questions.

Mr. TURNER. Thank you, Mr. Chairman.

And I want to thank both of you for what you're doing on a local level, what you're doing in taking some of the best practices and

describing it to others and highlighting some of the issues that you see that need to be resolved.

And one of the ones that I heard from you, as you were talking, that I think bears some additional discussion is the issue of when a property becomes a target for foreclosure and that process of foreclosure and, oftentimes, the resulting process of title problems that ensue and then the attempt to return that property back to productive use.

When I served as mayor of Dayton, before even the foreclosure crisis occurred, when we would have abandoned properties in neighborhoods I would have people ask me, you know, what is the biggest problem that you have with abandoned properties? And the answer sounded boring and esoteric, but it's the truth, and it's title. Tomorrow someone could not just go, grab that property and fix it up and put it back to productive use. There were usually highly complex title issues and problems as a result of the financial transactions that resulted in the property being abandoned and in foreclosure.

And now that we're seeing this massive foreclosure incidence, it's just compounding itself. And as you mentioned, Mr. Kildee, a lot of these properties being upside-down, when the lien values are greater than the property value itself, it causes even greater concern.

I saw there were many properties in our community that, when they were going in the process of foreclosure—sometimes even the family has left, perhaps even it's gone to sheriff's sale and no one has purchased it, perhaps it's gone to sheriff's sale and the bank itself has purchased it—that the lack of attention by the lender to the property or maintaining the value of the property had a huge negative impact on the neighborhood and, really, the future success of that property.

The lender's obligation, largely contractual, to the individual that they had the loan, they would have either lower increased liability to the lender based upon the lender having preserved the asset, but beyond that there was no obligation, other than just housing code and normal issues of condemnation if it became a threat.

Mr. Kildee, you mentioned the issue of Federal funding that can assist in that process, but I would like your additional thoughts on if there are things that we should be doing.

Obviously, the mortgage industry, a highly regulated industry. The foreclosure process is really a government-run process in order to sustain the financial transactions.

What are your thoughts on what you see of the failure of lenders to step to the plate and some of the things that you might know of that communities are doing that makes a difference? Mr. Kildee.

Mr. KILDEE. Well, lenders secure their financial interest in a property with a mortgage, which, from our point of view, and the way we modeled or created the Michigan law, is that mortgage interest is an ownership interest. And the rights of ownership come with significant responsibility.

I think you will probably hear some thoughts from some of the subsequent panel members, certainly Alan Mallach from the National Housing Institute—we were just talking about this subject—that we do need a system that recognizes that if a lender intends

to secure its financial interest in property with an ownership interest, with that ownership interest comes the responsibility of being a property owner. That means that building code violations should be the responsibility of that property owner.

And I know we've seen, certainly in Cleveland with the great work that Judge Pianka has done and certainly in New York, other housing court judges that have been willing to hold lenders responsible for that ownership interest. To me, that's critical.

Second, the point that you made initially on title, it's very important to create local authority to clarify title. And this is one—I know I'm sort of a one-note Johnny on land banks, but it's one of the things that land banks can do. The Michigan Land Bank Act allows us to expedite a quiet title procedure on any property that we have interest in in 90 days.

So, No. 1, identifying those owners of interest, holding them responsible as owners; and then, second, being able to take their interest away from them if they choose not to be responsible property owners. Whether it's a mortgage lender or the actual occupant of the property, the same standard ought to apply.

Mr. TURNER. Ms. Floreen.

Ms. FLOREEN. Yes, sir. I think one thing to recall, as well, is when you have an abandoned property with code enforcement issues because it's been left alone, even as a chain of title or just a sale is being addressed, it sends a message, it sends a message to every other property in that community.

It sends a message to the community that, "Well, you don't need to try. If you're on the edge, why not do it too? And why should we clean up that graffiti? And why should you cut your grass? And why should you fix those broken steps? And why should you respect your neighbor's need for noise control?" All the kinds of things, as you know, that make a huge difference in the quality of life within a community. "Why should children listen to their parents?"

I don't mean to overextend the analogy, but the fact remains that it sends a message to the whole community that we don't matter, that my community doesn't matter. And that is a very difficult thing to turn around.

As I said in my testimony, billions of Federal dollars have been spent on neighborhood revitalization to combat that very issue. And this just starts it all over again.

Mr. TURNER. Thank you, Mr. Chairman.

Mr. KUCINICH. I thank the gentleman.

I want to note that we've been joined by the Congressman from Massachusetts who represents the city of Lynn, among other areas.

Congressman Tierney, after Congresswoman Watson has a chance to ask questions, we'll go to you and then Mr. Higgins, if that would please the committee.

Congresswoman.

Ms. WATSON. Thank you, Mr. Chairman.

This goes to the Honorable Nancy Floreen.

In your town, in the communities, what happens at the point of contact with the consumer and the bank? I'm wondering how do these people get these subprime loans when they might make

$1,500 a month and the loan is for a property that costs $175,000? What happens at that point?

Ms. FLOREEN. Well, the issue of predatory lending is one that we've been struggling with in Maryland for quite some time. And, as you know, there is a tradeoff between the issue of access to credit fairly and in a proper way and access to credit that's designed to benefit the lender and, in many cases, the broker and does not achieve a desired social good and puts the purchaser in a position that they can really never dig their way out of.

Many of these issues are cultural. Many of the brokers are not regulated in the way that they should be.

And the big issue, as I think most people know, is the fact that there's no local financial institution interest in the property because of the way that these mortgages get bundled and sold. And who knows if people from Saudi Arabia end up holding the credit? It is an international market for items that used to be a local service and the local banks that would serve these folks.

Ms. WATSON. You led right into my next question that I wanted to know. And then also, Mr. Kildee, whose uncle is usually my seat-mate on the floor, a person I really respect. But, the two of you, have you seen an influx of foreign investment into the housing market? And if you have, how significant has that investment been, do you know? Either one.

Mr. KILDEE. I'm in a community where there's disinvestment. We don't have significant investment. What I have seen is something perhaps not quite as insidious as foreign investment but it's out-of-town investors. And, honestly, other than Ohio, California, Massachusetts and New York, we don't really want anybody investing in our properties. [Laughter.]

The issue for us has been this liquidation model that has applied previously to tax foreclosures and now is being applied to mortgage foreclosures, where the properties themselves are not treated as part of somebody's landscape but they're treated as security on some security that is bought and sold.

And so the concept behind this, sort of, liquidation approach that we're very worried about ignores the fact that the underlying asset sits next to some family and is a part of the fabric of a community. And that's problematic.

And that's why the notion of having local authorities making decisions about the actual disposition of the property, that consider the interest of the residents of the local community and the market conditions, I think is a better approach.

Ms. WATSON. I'm getting ready to hold a huge forum on this issue. And we have bankers, and we have all aspects of the consumer market and, as I said, the housing market. And I'm trying to get my staff to build it up so we can get a thousand people there, because this has been the No. 1 concern in areas of my district.

And I see the prey is on the lower socioeconomic areas and seniors. And people are losing their homes and calling my office, "What can I do?" So we want to get the information out there from the experts.

And we do have a set of bills going through that might address, but probably we need to do more overseeing of the regulators.

But that's why I ask you, Madam Councilwoman, what happens at that point of contact where a person will sign on that line and they have those balloon payments, you know, and they just can't handle them, and there we are, foreclosed?

Ms. FLOREEN. If I might observe, as well, Congresswoman Watson, consumer counseling is going to have to be an area where we devote tremendous attention to, and in many languages, and forcing people, really, to read the materials that they're provided and to be able to make the right financial decisions and understand the fiscal issues that they are getting themselves into.

Ms. WATSON. Just another comment, Mr. Chairman.

In California we have an Office of Consumer Affairs, and I'm thinking now about getting someone within my legislature to put in a bill that would require a division that will deal with property ownership and so on under the Department of Consumer Affairs. And we need that intermediate group where people can be educated before they sign on that line. So thinking that through, I think we'll have something that we can present.

Thank you, Mr. Chairman.

Thank you, witnesses.

Mr. KUCINICH. And I would like to have an ongoing discussion with the gentlelady about that. I think that we need to look for more solutions and dealing with it at a local level.

The Chair recognizes Congressman Tierney from Massachusetts. Thank you.

Mr. TIERNEY. Thank you very much.

Thank you both for being here today. I think you give a very good picture of what's going on out there.

Mr. Kildee, I probably don't have to but I want to add my voice to the chorus of people that tell you how much your uncle is respected and relied upon in this institution for his knowledge and his work ethic.

Mr. KILDEE. Thank you.

Mr. TIERNEY. So it's a pleasure to serve with him.

The legislation that we're talking about that may be vetoed, in a nutshell it talks about voluntarily writing down the value of the property and the mortgage on it in return for a guaranteed value of the security on that.

What is your opinion, in your respective communities, about whether or not lenders will, in fact, voluntarily participate in that program, as opposed to needing probably the stick of sorts of letting a bankruptcy judge have the same authority if they don't voluntarily participate?

Mr. KILDEE. Well, that's really the question that I think we're all trying to get our arms around. If there is some way—and this is obviously the legitimate role for a Federal, for Federal intervention.

For us, as the community—and I speak for people in Flint, and I speak for my land bank authority—if we can get these properties without having to purchase them at a price that essentially renders them useless to us, we want to get control of these properties. We have the capacity to manage them, but we can't take them by purchasing them for whatever the balance might be on a particular mortgage, because, in almost all the cases, the properties with sig-

nificant value have mortgage balances well above what our market will bear.

So, obviously, you put your finger on the problem.

Mr. TIERNEY. Do you have a feel for your community banking, establish with your lenders out that way as to whether or not they would voluntarily participate?

Mr. KILDEE. Local lenders, for sure. And in the case, for example, of Fannie Mae, I happen to chair the State land bank authority, and I purchased 184 mortgage foreclosed properties from Fannie Mae by proposing to them that we buy them for $175,000 each and competed against, I'm sure, what were more significant cash bids.

We were able to secure those properties because we have something that other purchasers don't have: the ability to manage that real estate, and to do it in a way that reduces the likelihood that more property in the surrounding landscape is going to see its values fall.

Any company that's going to be in business for more than the next 12 months better be thinking about how the disposition of their current assets is going to affect the remaining assets against which they have mortgages. And if they fail to do that, they do so at their own peril.

So thinking about these properties themselves as being the only properties that matter and the cash return that they might receive on those properties being the only number they need to be concerned with is a foolish, pennywise but pound-foolish approach. And that's what we're seeing some of them do.

In the case of Fannie Mae, they saw the light and were willing to work with us.

Mr. TIERNEY. Thank you.

Ms. FLOREEN. Congressman, I think from the banking perspective—of course the bankers can tell you—but I think it would be my expectation. What I'm told regularly is it's about time and it's about predictability.

Mr. TIERNEY. About time and what else?

Ms. FLOREEN. The time in which a property is not generating revenue for them, and predictability of the process and if there are clear guidelines, clear direction and the ability to move properties, which is what we all want. We want those properties back, occupied by families contributing to the community, in the speediest time available. That benefits all players.

Mr. TIERNEY. Well, thank you both.

Mr. Chairman, I yield back.

Mr. KUCINICH. I want to thank the gentleman from Massachusetts and thank the panelists.

The subcommittee will be in contact with you. And one of the things that we're going to be looking at is to try to quantify the transfer of wealth that's occurring here. Because the underlying question—and to members of the subcommittee, to my colleagues Ms. Watson, Mr. Tierney, Mr. Cummings—the underlying question that we're moving toward here is that there has been a massive transfer of wealth upwards in the hands of a few, taking money away from people whose greatest investment is their home, taking money away from communities. And, in some of your remarks, Mr. Kildee you got into that.

I want to thank this panel. We're going to be looking at that further, because this is bottom-line rock-bottom issue here, this transfer of wealth that's going on. It's extraordinary. Thank you—we will be in touch with you—Mr. Kildee, Ms. Floreen, for your testimony, for your willingness to answer questions.

We're going to move on to the next panel. And as we're moving on to the next panel, I want to say how pleased we are to be joined by the Congressman from Maryland, and particularly Baltimore, Congressman Elijah Cummings, who has been a critical part of the work of this subcommittee in looking at all issues that relate to the economy of cities and to the issues that relate to making sure that government is truly functioning for people in the inner-city.

So, Mr. Cummings, thank you for joining us.

And we're now going to move to the next panel. We're fortunate to have outstanding witnesses on our second panel.

I would ask that you be seated.

We have Ms. Vicki Been, who is a professor of law and public policy at New York University School of Law. She's also the director of the Furman Center for Real Estate and Urban Policy. Her areas of research include affordable housing, land use, and predatory lending.

Ms. Been's research has been published in numerous journals, including a 2004 article in Cityscape entitled, "Impact Fees and Housing Affordability."

Next, Dr. Phyllis Betts. As Dr. Betts is moving to her position at the witness table, Dr. Betts is the director of the Center for Community Building and Neighborhood Action at the University of Memphis. She has over 10 years of experience working with community development organizations and agencies. Her work evolves around sustaining neighborhood housing markets and enhancing quality of life in low- to moderate-income neighborhoods.

Mr. John Talmage. Mr. Talmage is the president and CEO of Social Compact, Inc. Under his leadership, Social Compact performs market research and analysis of inner-city neighborhoods throughout the country. The goal of this effort is to generate new tools and practices that will contribute to innovation in the field of community development.

Prior to joining Social Compact, Mr. Talmage served as the deputy director for economic development for the city of New Orleans, where the focus of his work was business development.

I want to thank the witnesses for appearing before the subcommittee today.

Just to let you know, it's our policy to swear in witnesses. I would ask that you stand and raise your right hands.

[Witnesses sworn.]

Mr. KUCINICH. Let the record reflect that each witness answered in the affirmative.

And I would ask, as in the previous panel, that each witness give a statement 5 minutes or less in duration. Your entire statement will be included in the record of the hearing. I am grateful for your presence here.

And I would ask that we begin with Ms. Been. Please proceed.

STATEMENTS OF VICKI BEEN, ELIHU ROOT PROFESSOR OF LAW AND PROFESSOR OF PUBLIC POLICY, CO-DIRECTOR, FURMAN CENTER FOR REAL ESTATE AND URBAN POLICY, NEW YORK UNIVERSITY SCHOOL OF LAW; PHYLLIS G. BETTS, DIRECTOR, CENTER FOR COMMUNITY BUILDING AND NEIGHBORHOOD ACTION, SCHOOL OF URBAN AFFAIRS AND PUBLIC POLICY, UNIVERSITY OF MEMPHIS; AND JOHN TALMAGE, PRESIDENT AND CEO, SOCIAL COMPACT

STATEMENT OF VICKI BEEN

Ms. BEEN. Chairman Kucinich and all the members of the subcommittee, I am honored to be here today to share with you findings from the Furman Center's research on the external effects of mortgage foreclosures and vacant properties.

Few urban problems have been more vexing or more threatening than the huge number of mortgage foreclosures plaguing our communities. To understand better how and whether the Government should intervene in this crisis, the Furman Center has undertaken several studies to examine the external costs that foreclosures impose.

Foreclosures obviously harm the homeowners who are threatened with losing their homes, as well as their creditors. But if foreclosures also harm third parties, such as neighbors, the broader community and the renters of the properties that are in foreclosure, the justification for Government intervention in the crisis becomes all the more compelling.

To assess the external effects foreclosures have on neighbors and the broader community, we examined the impact that the filing of a foreclosure notice has on the sales prices of nearby properties. And to assess the harms foreclosures might impose on renters in buildings going into foreclosure, we examined the characteristics of the buildings that were entering foreclosure in 2007 in New York City and estimated how many of those buildings housed tenants who would be dislocated by the foreclosure.

I will briefly describe our findings on each of those issues.

Our research shows that foreclosures depress the sales prices of nearby properties. Properties near homes and buildings that have entered the foreclosure process, on average, sell at lower prices than comparable properties in the same neighborhoods that are not near homes in foreclosures.

Foreclosures in New York City are highly concentrated in specific neighborhoods. In order to assess the effects that foreclosures had on the neighboring properties, we separated New York City's neighborhoods into two groups: high-exposure neighborhoods in which the median property sold was near 15 properties that were in the foreclosure process; versus low-exposure neighborhoods in which the median home sale was near only one property.

In the low-exposure neighborhoods, the sales prices of homes within 500 feet of just one or two properties for which a foreclosure notice had been filed in the prior 24 months was almost 2 percent lower than the prices of similar properties in the same neighborhood but not near a foreclosure.

Sales prices of homes within 5,000 feet of three to five properties that were in foreclosure were almost 3 percent lower than the

prices of comparable properties that were not near a foreclosure. In the high exposure neighborhoods, properties again sold for less than comparable properties in the same neighborhood but near fewer recent foreclosures. The discount was higher for properties near larger numbers of foreclosures.

Our work accordingly provides strong evidence that neighbors bear significant costs when a homeowner loses his or her property to foreclosure. Local governments in turn lose tax revenues. Efforts to help stem the tide of foreclosures and to assist local governments in putting those foreclosed properties back into the hands of responsible families accordingly may be justified by the external effects that foreclosures have on property values.

Our research also documents that foreclosures have an impact on another group of collateral victims. Our data on notices of foreclosure filed in 2007 in New York City reveals that 60 percent of the properties going into foreclosure in 2007 were two- to four-family buildings or multifamily buildings.

A conservative estimate is that those buildings house at least 15,000 renter households. If those properties are sold at auction, those households will face eviction and will bear the cost and dislocation of finding a new home.

New York City isn't exceptional in this regard. Other research has also documented that multifamily buildings make up a significant portion of the foreclosures throughout the northeast.

Our results show that foreclosures not only harm the homeowners and creditors involved but also hurt neighboring properties, the community itself, and the tenants in those buildings. Whatever the outcome of the debate over the desirability of assisting homeowners facing foreclosure or their creditors therefore, there is justification for intervening in the foreclosure crisis to protect those third parties who our results reveal are bearing a significant part of the cost of foreclosures.

Thank you.

[The prepared statement of Ms. Been follows:]

External Effects of Concentrated Mortgage Foreclosures: Evidence from New York City

Testimony of Vicki Been
Elihu Root Professor of Law
Director, Furman Center for Real Estate and Urban Policy
New York University

Before
Committee on Oversight and Government Reform
Subcommittee on Domestic Policy

Honorable Dennis Kucinich, Chair
May 21, 2008

Chairman Kucinich, Ranking Member Issa, and all the members of the Subcommittee, I am honored to be here today to share with you findings from the Furman Center's research on the external effects of concentrated mortgage foreclosures. My name is Vicki Been, and I am the Elihu Root Professor of Law at New York University School of Law and director of the Furman Center for Real Estate and Urban Policy. The Furman Center is a joint research center of NYU's School of Law and its Robert F. Wagner School of Public Service, and is a member of the National Neighborhood Indicators Partnership. Founded in 1995, the Center brings the talents of both our law faculty and our urban economics faculty to bear on urban problems, and has become one of the nation's leading academic research centers devoted to the public policy aspects of land use, real estate development and housing.

As the national mortgage crisis has worsened, an increasing number of communities are facing declining housing prices and high rates of foreclosure. Central to the call for government intervention in this crisis is the claim that foreclosures not only hurt those who are losing their homes to foreclosure, but also harm others – neighbors, communities, and tenants – by reducing

the value of nearby properties and in turn, reducing local governments' tax bases, and by displacing tenants. The extent to which foreclosures do in fact drive down neighboring property values or displace tenants, and how those impacts may vary according to neighborhood characteristics and local housing markets, thus have become crucial questions for policy-makers as they struggle to address the rising tide of foreclosures throughout the country.

In part because of the difficulty of obtaining necessary data, few empirical studies have examined the relationship between foreclosures and surrounding property values, and those that have addressed the issue have been unable to resolve the critical question of causality—that is, whether foreclosures drive down surrounding home prices or whether foreclosures simply tend to occur in neighborhoods with lower-value homes. The Furman Center has tried to respond to the pressing need for information about the effects of foreclosures by examining the impact that the filing of a foreclosure notice (a "*lis pendens*", or LP) has on the sales prices of nearby properties.[1] Our research offers several methodological improvements over prior studies that help to shed light on the causal relationships at play.

In addition, the Furman Center has examined the characteristics of the approximately 15,000 buildings that entered foreclosure in 2007 in New York City to assess whether foreclosures are affecting tenants. I will describe our research on both these issues in turn.

The Effects Foreclosures Have on the Value of Neighboring Properties:

We have provided background on the foreclosure process in New York City, along with a detailed explanation of our data and methodology, in Appendices A and B. In brief, we examine data on foreclosure starts and sales prices over a six year period, as opposed to the one year of sales data other studies typically have used. We take into account unobserved characteristics of

[1] Our research on the impacts foreclosures have on neighboring properties was supported through a grant by the Surdna Foundation.

the neighborhood, as well as broader economic conditions. Our model accordingly does a better job of controlling for the various neighborhood characteristics that may affect both sales prices and the likelihood that a foreclosure will occur nearby, which allows us to isolate the impacts foreclosure starts have on prices from the impacts of other market conditions. Moreover, we study the impacts of foreclosures during a period of price appreciation in the New York City housing market.

Before I share our results, it is useful to review the various hypotheses about why foreclosures may have a negative impact on surrounding housing prices. First, property owners who are in default on their mortgages may be less likely to maintain or upgrade their properties, either because they have less incentive to maintain property they may lose, or because the mortgage default results from financial problems that also constrain the property owners from taking appropriate care of their homes. Properties may start to appear rundown as a result, which may make the surrounding homes less desirable. Second, after completion of foreclosure proceedings and eviction of the delinquent borrower, the property may sit vacant and suffer further physical decline. Vacant properties are likely to depress surrounding property values because they contribute to neighborhood blight, may attract vandalism and crime, and more generally signal that the neighborhood is not stable. Even if the vacant properties are well maintained and do not attract criminal or other undesirable activities, they add to the local supply of available units, and under the law of supply and demand, will thus depress property values. Third, distressed properties sold either at foreclosure auctions or pre-foreclosure sales may be more likely to be sold to investors and become renter-occupied, which may lead to lower levels of maintenance even after the properties are re-occupied. Finally, properties with distressed loans are likely to sell at a discount – both at pre-foreclosure sales and at foreclosure auctions – thus affecting the price of "comparables" used to estimate neighboring property values.

If foreclosures are clustered by neighborhood, the magnitude of these negative effects is likely to increase. Further, the size of these effects is likely to differ according to the strength of the housing market. Foreclosed properties are more likely to remain vacant for longer periods in stable or declining housing markets than in appreciating markets.

Our research shows that foreclosures have a depressing effect on nearby sales both in neighborhoods with few foreclosures and neighborhoods with many concentrated foreclosures. Properties near recent foreclosure starts on average sell at lower prices than comparable properties in the same neighborhoods that are not near foreclosure starts. As expected, the size of the price impact generally increases with the number of nearby foreclosure starts, although the marginal impact of each additional foreclosure decreases once there is a concentration of foreclosures in a neighborhood.

Specifically, we find that:

- Foreclosures in New York City are highly concentrated in specific neighborhoods. We separated New York City's neighborhoods[2] into two groups: in "high-exposure" neighborhoods, the median property sold was within 1,000 feet of fifteen properties for which notices of foreclosure had been filed; in "low-exposure" neighborhoods, the median home sale was within 1,000 feet of only one property subject to a *lis pendens*. High-exposure neighborhoods tend to have a greater proportion of black and Hispanic residents, lower median incomes, lower median sales prices and higher rates of subprime lending than low-exposure neighborhoods.

[2] For the purposes of our research, we use the City's 59 community district (CD) boundaries to identify distinct neighborhoods. Staten Island is not included in our data set because *lis pendens* data for the borough was unavailable for the time period we studied.

- In low-exposure neighborhoods, the sales prices of homes within 500 feet of just one or two properties for which a *lis pendens* had been filed in the prior 24 months were 1.8 percent lower than the prices of similar properties in the same neighborhood but not within 500 feet of any recent foreclosure start, all else equal. Sales prices of homes within 500 feet of three to five properties for which a *lis pendens* had been filed in the past two years were 2.8 percent lower than the prices of comparable properties not within 500 feet of any recent foreclosure start. We found that homes slightly further from foreclosure starts (500 to 1,000 feet) also sold for significantly less than comparable properties, but estimated price reductions were smaller.
- In high-exposure neighborhoods, properties near nine to nineteen recent LPs sold for 2.5 percent less than comparable properties in the same neighborhood but near fewer than nine recent LPs. Properties near twenty or more recent LPs sell for approximately 3.7 percent less than comparable properties near less than nine recent LPs, all else equal. The median sales price in high-exposure neighborhoods during our study period was approximately $216,000, implying that being close to twenty or more LPs is associated with a discount of approximately $8,000 in sales price.
- Overall, the results suggest that in low-exposure neighborhoods, prices are sensitive to even a small number of nearby LPs. In high-exposure neighborhoods, almost all sales occur near a large number of recent LPs, so we cannot test for the effects of being near only a few LPs. However, in these high-exposure neighborhoods, we do find significant price discounts from being near a larger than average number of recent LPs.

Explaining Differences in the Results of Research on the Effects Foreclosures Have on Neighboring Properties:

These numbers, while staggeringly high in terms of their impact on America's neighborhoods and upon the wealth available to America's homeowners, are lower than some of the estimates that have been discussed in the debate over how to respond to the housing crisis. In the most frequently cited study, Dan Immergluck and Geoff Smith find that each foreclosure within one-eighth of a mile of a single-family home is associated with a decline in property values of approximately 1 percent.[3]

The disparity between our estimates and theirs may be the result of several factors. First, there may be differences in the market conditions in their study area (Chicago) and ours (New York City) that affect the impact foreclosures have. Second, our study evaluated impacts during a different time period (2000 – 2005) than theirs (1997 – 1999). Third, our data allowed us to make several improvements over the methodology Immergluck and Smith used. Their research attempted to identify the effects of foreclosures by examining whether properties sell at lower prices if a foreclosure has occurred nearby in the two years prior to the sale. However, they looked only at price differences after the foreclosure, and did not account for possible price differences before the foreclosures occurred. It is likely that there are unobservable differences between properties and neighborhoods that are close to a foreclosure at some point in time and properties (and their neighborhoods) that are not. If the characteristics of properties that determine the likelihood of being near a foreclosure also are correlated with sales prices, then only measuring the effect of foreclosures within the two-year window will produce biased estimates. Because we have data on foreclosure starts and sales prices over a longer period of

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[3] Immergluck, Dan and Geoff Smith. 2006. "The External Costs of Foreclosure: The Impact of Single-Family Mortgage Foreclosures on Property Values." *Housing Policy Debate.* 17(1): 57-79.

time (six years), we are able to control for whether a foreclosure occurs near each sale at any time within six years, not just in the two years immediately before the sale. The longitudinal structure of our data also allows us to control for unobserved characteristics of the neighborhood that do not change over time (what we call zipcode "fixed effects") as well as to control for broader economic conditions that do vary over time.

To understand whether the difference between our estimates and those of Immergluck and Smith is driven by New York City's market, which was appreciating during the study period, or by methodology, we replicated their research using our data. Using their methods, we find that a foreclosure start within one-eighth of a mile is associated with a 0.2 percent reduction in property values (as compared to their 1 percent estimate). Because we replicated their methods as closely as possible, the difference between their larger estimates and our smaller estimates must be driven by differences between the Chicago and New York City housing markets or differences between the housing market in 1997 and 1998 (the time period Immergluck and Smith studied) and the later six year period of 2000 to 2005 that we studied.

But the improvements in methodology that we were able to make also explain some of the difference. The results of our methodology are not directly comparable to the Immergluck and Smith estimates because their work assumes that each additional foreclosure in a neighborhood has the same effect as the prior foreclosure. It is highly unlikely, however, that each additional foreclosure in a neighborhood generates the same impact. Indeed, as described above, our estimates suggest that while the first few foreclosures in a neighborhood generate fairly significant impacts, subsequent foreclosures have a much smaller marginal impact.

Despite the differences between the study areas and between our methodologies, however, both our work and that of Immergluck and Smith provide strong evidence that neighbors, and local governments, bear significant costs when a homeowner loses his or her

property to foreclosure, and that efforts to help stem the tide of foreclosures and to assist local governments in putting foreclosed properties back into productive use may be justified by the external effects that foreclosures have on neighboring properties.

The Effects of Foreclosures on Tenants:

Our research also documents that foreclosures have an impact on another group of collateral victims. As detailed in Appendix C, we recently documented that in New York City, 60 percent of the properties going into foreclosure in 2007 were two- to four-family or multi-family buildings, representing at least 15,000 renter households (or approximately 38,000 individuals). If these properties are sold at auction, most of these households will face eviction. Recent research by the National Low Income Housing Coalition has highlighted this problem in other regions as well, specifically finding that multi-family buildings made up one-third of foreclosed properties in New England.[4]

What Do Our Findings Suggest About How Resources Should be Targeted?

Our results show that foreclosures not only harm the homeowners involved, but also hurt neighboring properties, the community itself, and tenants. Whatever the outcome of the debate over the desirability of assisting homeowners facing foreclosure (or their creditors), therefore, there is a justification for intervening in the foreclosure crisis to protect neighbors, tenants and communities, who our results reveal are bearing a significant part of the cost of foreclosures.

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[4] Pelletiere, Danilo and Keith E. Wardrip. "Properties, Units, and Tenure in the Foreclosure Crisis: An Initial Analysis of Properties at the End of the Foreclosure Process in New England." National Low Income Housing Coalition, Research Note #08-01. May 6, 2008. Also available at http://www.nlihc.org/doc/RN-08-01-Multi-Unit-Foreclosure-FINAL-05-06-08.pdf.

Our results also can help policy-makers allocate limited resources to local governments confronting rising foreclosures. One preliminary caution: as noted above, the comparison of our results to those of Immergluck and Smith's show that there is considerable variation in the effects foreclosures may have in different cities, and at different times. Our results also show that even within New York City neighborhoods, the effects of foreclosures vary. Those variations suggest that we cannot necessarily extrapolate the experience of one housing market to another, and caution against developing policies that treat all foreclosures equally.

Nevertheless, our results suggest some of the ways in which programs to address the foreclosure crisis should be targeted. First, the results make clear that even in appreciating markets, where properties are unlikely to sit vacant for long periods after a foreclosure, neighbors and tenants suffer when properties go into foreclosure. While limited resources must be targeted to the areas most in need, it would be a mistake to think that so-called "hot" markets are immune from the negative effects of foreclosures.

Second, we know from previous research, and from the experience of communities around the country, that vacant properties can damage neighborhood property values and contribute to other problems such as crime. Programs to minimize the number of vacant properties resulting from foreclosures accordingly are critically necessary. In work published several years ago, Furman Center researchers found that properties near to vacant properties sold for significantly less than otherwise comparable properties that were not close to vacant properties. Specifically, properties adjacent to abandoned or vacant buildings typically sold for 28 percent less than comparable properties located further away but still in the same

neighborhood. The negative associations were significant at distances up to 2,000 feet away from the abandoned property.[5]

Third, any effort to target resources to those communities most in need must take into account not only existing foreclosures, but the probability that the neighborhood will suffer foreclosures in the future. Data about foreclosures themselves are notoriously unreliable and subject to variation from jurisdiction to jurisdiction. But even if the data about foreclosures were perfect, by the time foreclosures are filed, it often will be too late for local governments to implement cost-effective ways to avoid or minimize the external effects of foreclosures. Any formula allocating aid to local governments accordingly should use all data available to predict where foreclosures are likely to occur, rather than looking only at where foreclosures already have occurred.

Several indicators are reliable harbingers of foreclosures to come. First, there is a substantial relationship between the prevalence of subprime lending and the prevalence of foreclosures.[6] In New York City, among the ten community districts with the highest rates of subprime lending, our research shows that seven of them also were among the ten community districts with the highest rates of foreclosure.[7] Therefore, the formula for allocating aid should take into account the prevalence of subprime lending in a community. Second, other forms of risky lending also are associated with higher than average rates of foreclosure. For example, the proportion of borrowers taking out second liens, or piggyback loans, is associated with higher

[5] Michael H. Schill, Ingrid Gould Ellen, Amy Ellen Schwartz, and Ioan Voicu, "Revitalizing Inner-City Neighborhoods: New York City's Ten Year Plan for Housing," Housing Policy Debate 13(3), 2002: 529-566.
[6] For example, the Federal Reserve Bank of New York recently analyzed existing mortgage loans n New York City and found that, as of December 2007, approximately 6 percent of subprime fixed rate first mortgages and approximately 20 percent of the more common subprime adjustable rate first mortgages were in foreclosure. In both cases, these foreclosure rates exceed the corresponding national rates. See http://www.ny.frb.org/regional/subprime.html
[7] See Amy Armstrong et al. 2008. State of New York City's Housing and Neighborhoods 2007. New York: Furman Center for Real Estate and Urban Policy.

rates of foreclosure.[8] Similarly, the proportion of borrowers who are refinancing even when increasing interest rates are making refinancing financially unattractive should be a danger signal.[9]

Finally, the plight of renters that have been or will be displaced from units they rented in buildings that go into foreclosure should be factored into formulas for targeting aid to communities.

Conclusion:

Our research shows that the foreclosure crisis is affecting not just the homeowners who are unable to pay their mortgages, but also is imposing significant costs upon the neighbors and tenants of those owners, as well as the communities in which the properties going into foreclosure lie. The costs inflicted upon those collateral victims may justify government intervention in the foreclosure crisis, and should be considered in decisions about how to target aid to local governments confronting the crisis.

[8] See http://www.ny.frb.org/regional/subprime.html

[9] See generally, Amy Armstrong et al. 2008. State of New York City's Housing and Neighborhoods 2007. New York: Furman Center for Real Estate and Urban Policy.

Appendix A: Foreclosure Process in New York City

The mechanisms by which defaulted loans can create negative spillovers into their neighborhoods and at what point in time these spillovers occur depend on the details of the foreclosure process. Since the foreclosure process differs considerably across states, I will offer a brief review of how foreclosures work in New York City, focusing particularly on points during the process when information becomes available to third parties.

The first stage of loan distress, mortgage default, occurs when the borrower fails to make the mortgage payment for a period of time specified in the mortgage contract. Once a borrower defaults on the mortgage, lenders then have several options, including loan restructuring, forbearance, or beginning the process to reclaim the property, described below. We do not observe when a borrower initially defaults or any actions taken by the lender prior to the *lis pendens* filing, since no public notice or third party involvement occurs in the initial stage of default. Thus, for the purposes of our analysis, we treat the date of the *lis pendens* filing as the starting point for the foreclosure process.

After a mortgage has gone unpaid for a minimum of three consecutive months, the lender can file a *lis pendens* (LP), essentially a notice of the intention to sue the property owner and reclaim the property if the loan is not repaid.[10] The *lis pendens* is filed with the county clerk's office and is therefore a public record. A number of private data vendors collect and sell information on LP filings, which prospective real estate investors use to identify properties for potential purchase.

After the *lis pendens* has been filed, the borrower may attempt to prevent the property from being foreclosed by restructuring the loan with the existing lender, refinancing the property

[10] *Lis pendens* can be filed for a number of reasons other than default on mortgage loan, including unpaid taxes, unpaid condominium fees, or mechanic's or contractor's liens. We include only *lis pendens* filings that result from mortgage default.

with a different lender, or selling the property to a third party and satisfying the loan. The borrower may also turn over the deed to the property to the lender in lieu of paying off the loan. Any of these actions to avoid a foreclosure auction can be observed through documents filed in the public record.

In the third and final stage, if the borrower and lender do not reach an agreement to satisfy the outstanding loan after the filing of a *lis pendens* notice, then the lender may request that the court appoint a referee (an attorney who ultimately conducts the foreclosure sale) and schedule an auction. The judge then signs a Judgment of Foreclosure and Sale that directs a Notice of Sale to be published. A notice of the property's pending sale – including the date, time, and location of the auction, the property address, and the names of the borrower and lender – must be published in newspapers or other media for four successive weeks prior to the auction. The announcements of foreclosure auctions are thus available to any party that chooses to search the papers; several data vendors also collect and sell this information.

At the auction itself, the property will be sold to the highest bidder. The original lender will generally purchase the property if no private investor bids higher than the amount of the outstanding loan. The winning bidder must pay 10 percent of the purchase price immediately after the auction, and is required to pay the balance within thirty days. The sale price, along with the name of the new owner, is recorded as part of the public record in the deed transfer.

If the lender takes ownership of the property, either through an agreement with the borrower during pre-foreclosure or at the foreclosure auction, the lender will typically re-sell the property to recover the unpaid loan amount in what is known as a "Real Estate Owned" (REO) sale. The transfer of property ownership back to lender, as well as the subsequent REO sale price, is recorded as part of the public record.

Appendix B: Data and Empirical Strategy

To identify the effect of foreclosure starts on neighboring property values, we use a variation of hedonic regression analysis, controlling for property and neighborhood characteristics. The general form of the regression is shown in Equation 1 below:

(1) $LPRICE_{ijt} = \beta_0 + \beta_1 \mathrm{Re}\,centLP_{ijt} + \beta_3 EverLP_{ij} + \beta_4 \Pr opChars_{ij} + Zip_j + Boro * quarter_t$

in which $LPRICE_{ijt}$ is the log per unit sales price of property i in zipcode j in quarter t; $\mathrm{Re}\,centLP_{ijt}$ is an indicator of the presence (or number) of LP filings within 1000 feet of property i during the period of time 24 months prior to the sale; $EverLP_{ij}$ is a dummy variable indicating the presence of an LP within 1000 feet of the sale at any time between January 1 2000 and December 31 2005; $\Pr opChars_{ij}$ is a vector of characteristics describing property I, including size, age, and building class; Zip_j is a set of zipcode fixed effects and $Boro * quarter_t$ is a set of borough-quarter-year fixed effects. Data sources and brief descriptions of each variable are shown in Table 1.

Our dependent variable is the actual per-unit sales price of residential properties in New York City, provided by the City's Department of Finance.[11] We restrict the sales to years in which we have data on LPs during the relevant periods. Our data on LP filings begin as of January 2000 and end in December 2005. Thus for sales beginning July 1 2001, we have at least eighteen months of prior LP filings. We end the period of analysis with sales through September 30, 2005, so that we also have LP filings in the subsequent three months.

The regressions include a number of variables standard to hedonic price analysis, specifically physical property characteristics, fixed effects for zipcodes and period of sale. Property characteristics include the building type, age, size, lot shape and whether the unit has

[11] We exclude non-residential property sales and sales of coops, which are counted as shares in a corporation.

recently been altered. To control for locational amenities and neighborhood characteristics, such as proximity to transportation, quality of local schools and other public services, demographic and economic characteristics of the population, we include a series of fixed effects for the zipcodes in which the sale is located. We also include fixed effects for the quarter of sale, interacted with borough to control for time-varying economic trends that may differ by borough.

To identify whether each sale is likely to be affected by mortgage foreclosure starts, we draw upon property-level LP filings between 2000 and 2005 in four of the five NYC boroughs (Staten Island did not report LP data in a comparable fashion). Data on LPs from Bronx, Kings, New York and Queens Counties were purchased from Public Data Corporation, which collected these data from the county court registers. We exclude all LPs that are not related to mortgage foreclosures (such as tax liens, mechanics liens and housing code violations) and LPs filed on non-residential properties. It is fairly common for multiple LPs to be filed on the same property in a short period of time; we assume that the first filing indicates the beginning of the period of financial distress and drop any subsequent LPs filed on that property within 365 days by the same plaintiff. We assume that one of the mechanisms by which LPs create spillover affects is physical deterioration; because condominium units that enter foreclosure are less likely to display signs of distress that will be visible outside the building, we also exclude LPs on condominiums.[12] Most of the remaining properties on which LPs were filed are one- to four-family buildings, and a small number of multifamily buildings.

Table 2 shows the number of LPs in each borough by year, while Table 3 shows the distribution of LPs by property type. We calculate several different indicators of the extent of foreclosure activity around each sale. The simplest measure is a dummy variable that indicates whether any LP occurred in the 24-month period previously described within 1000 feet of the

[12] Some LPs are dropped from our analysis because they are missing the geographic indicators needed to match with sales locations, but these are quite small numbers and are unlikely to affect our results.

sale. The distribution of LPs near each sale is highly skewed; therefore in several specifications, we use a series of categorical variables for the number of LPs within 1000 feet.

There are several empirical and theoretical challenges to identifying possible effects of LPs on housing prices. The primary concern is that LPs are more likely to occur in neighborhoods with initially lower property values, making it difficult to determine the direction of causality. As shown in Figures 1, 2 and 3, LPs are more frequent in neighborhoods with low-income and minority populations and high rates of subprime lending. In New York City, LPs are highly concentrated geographically, also hindering a clean identification. As shown in Figure 4, sales that are within 1,000 feet of at least one LP are likely to be near large numbers of LPs. Thus it is quite difficult to compare the price of a sale near no LPs with the price of a sale near one or more LPs within the same zipcode. If LPs have a cumulative effect on prices, then identifying the magnitude of being near exactly one LP should not be extrapolated linearly to determine the effect of being near multiple LPs, particularly because sales near many LPs are likely to occur in quite different neighborhoods from those with isolated LPs.

We employ several different techniques to correct for potential selection bias and other challenges to identification. In specifications using the full sample of sales, in addition to looking at the number of LPs that occurred in the previous 24 months, we control for whether an LP was issued within 1000 feet of the sale at any time during the six year period for which we have data (2000 to 2005), and for some specifications, whether at least five or ten were issued. Over 90 percent of sales across the city had at least one LP within 1000 feet at some time during those years (over 97 percent in Brooklyn and Queens, just over half in Manhattan). This suggests that in most boroughs and many CDs, proximity to at least some foreclosure activity is almost universal, with the variation arising from timing and intensity of activity.

However, these statistics of proximity to LPs at the borough and CD level may obscure considerable differences in the prevalence of foreclosures resulting from selection bias at smaller levels of geography. One approach is to segment the sample by the prevalence of LPs in the CD and test separately for effects of LPs in high- and low-exposure CDs. We define high- and low-exposure CDs by calculating the rate of LPs per 1,000 owner-occupied housing units (using census data from 2000 on tenure rates and housing stock). CDs with fewer than twenty LPs (over the six year period) per 1000 owner-occupied units are defined as low-exposure, while those with fifty or more LPs are defined as high exposure.[13] As shown in Table 4, in high-exposure CDs, almost all sales are within 1000 feet of at least one LP in the 24-month window, and most are near multiple LPs. In these regression specifications, identification of the effect of LPs comes from variation in number of LPs within the 24-month window; we cannot test for the effect of a single LP compared to none in this sample, but can test for the marginal effect and differences between median prevalence of LPs and unusually high prevalence. In the low-exposure CDs, we are able to test for the effect of being near one LP, compared to being near none. Not surprisingly, low- and high-exposure CDs differ quite a bit in their economic and demographic characteristics. In particular, as shown in Table 5, CDs with very high rates of LPs have lower median housing prices initially, lower median incomes, a larger share of black residents and higher exposure to subprime lending. This supports the hypothesis that lower-value neighborhoods are more vulnerable foreclosure starts.

Besides econometric difficulties, identifying the effects of LPs is complicated by limited information over the intermediate and final outcomes of the distressed property and the length of time needed to resolve each LP. As described in Section 3, magnitude and duration of spillover effects depends on extent and timing of visible signs of deterioration, when and to whom the

[13] These cutoffs were identified based on the distribution of the variable, to provide roughly similar sized groups. Neither the descriptive statistics nor the regression results are sensitive to moderate changes in the cutoff points.

property is sold, when and by whom it is occupied, etc. Unfortunately we do not have data that allow us to determine the outcomes of individual LPs and so cannot examine differential effects by outcomes, but this is an area that should be pursued in future research.

Table 1: Variable definitions and data sources

Variable	Comments and source
Dependent variable	
Log(Price/unit)	Log(price per unit), constant 2005 $. Source: NYC DOF
Proximity to LP measures	
Source: PDC, DOF	
Any LPs	Any LPs within 1000 feet of sale, 24 months
1-2 LPs (etc.)	Dummy = 1 if 1-2 LPs within 1000 feet, 24 months (comparison group varies by specification)
Any LP 2000-06?	Any LPs within 1000 feet of sale, 2000-05
Hedonic characteristics	
Source: RPAD	
unitage	Unit age, years.
noyrblt	Unit age missing flag
sqftunt	Square feet of unit
bldgs	Number of buildings on lot
numunits	Number of units in building
sf_att	= 1 if SF attached, 0 ow
twofam	=1 if two-family
mf3_4	= 1 if 3-4 family building
mfwalkup	= 1 if 5+ family multifamily, walkup
elnocnd	= 1 if elevator multifamily, not condo
cndnoel	= 1 if condo, no elevator
cndelev	= 1 if condo, elevator building
mixed	= 1 if mixed residential-commercial building
oddshape	= 1 if lot is oddly shaped
garage	= 1 if garage
extended	= 1 if building was extended
xcorner	= 1 if corner lot
altered2	= 1 if building had recent significant alteration
Fixed effects	
Boro-year-qrtr	Dummy variables for each borough-quarter-year of sale
Census tract/ZIP	Dummy variables for each census tract or ZIP code

Table 2: Number of LPs by borough and year

	2000	2001	2002	2003	2004	2005	Total
Bronx	755	967	1,052	979	871	775	5,399
Brooklyn	2,742	2,466	2,944	2,861	2,455	2,504	15,972
Manhattan	268	155	146	123	95	84	871
Queens	2,553	2,556	2,637	2,482	2,330	2,372	14,930
Total	6,318	6,144	6,779	6,445	5,751	5,735	37,172

Source: Furman Center calculations based on data from Public Data Corporation (PDC)

Table 3: Number of LPs by building type (2000 – 2005)

One-family	14,376
Two-family	14,547
Walk-up apartments	7,753
Elevator apartments	73
Condominiums	1
Residential-mixed use	1,795
Total	38,545

Source: Furman Center calculations based on data from PDC and NYC Department of Finance

Table 4: Segmenting Community Districts (CDs) by LP Prevalence

		All CDs	Low LP CDs	High LP CDs*
LPs/1000 owner-occupied units (2000-05)				
	Median	30	11	102
	Range	0-284	0-20	50-284
Number of CDs		56	22	22
Number of sales		91,863	35,129	38,498
Median sales price		268,435	403,200	216,087
Sales w/ LPs in 1000 ft				
LPs/sale (24 mos)	Median	4	1	15
	Range	0-90	0-16	0-90
% sales near LP (24 mos)		82.5%	62.1%	98.0%
% sales near LP (2000-06)		91.8%	81.5%	99.6%
Sales w/in 250 ft of 1+ LP				
LPs/sale (24 mos)	Median	0	0	1
	Range	0-16	0-8	0-16
% sales near LP (24 mos)		36.7%	11.6%	62.5%
% sales near LP (2000-06)		57.8%	27.5%	86.4%

* Excludes Parkchester/Soundview

Source: Furman Center calculations based on data from PDC and NYC Department of Finance

Table 5: Characteristics of CDs by Exposure to LPs (2000)

	All CDs	Low LP	Middle LP	High LP
Number of CDs	56	22	11	23
Median Income	$37,038	$47,159	$32,789	$29,390
% subprime home purchase loans	4.0%	0.8%	2.6%	7.7%
% Black	26.7%	7.1%	18.1%	49.7%
% White	33.7%	57.8%	34.5%	10.4%
% Hispanic	29.3%	19.2%	36.4%	35.5%
% Asian	10.2%	16.0%	11.0%	4.4%
% Poor	23.0%	15.1%	24.8%	29.8%
% Unemployed	11.1%	6.9%	10.5%	15.4%

Source: Furman Center calculations based on data from the U.S. Census and the Home Mortgage Disclosure Act (HMDA)

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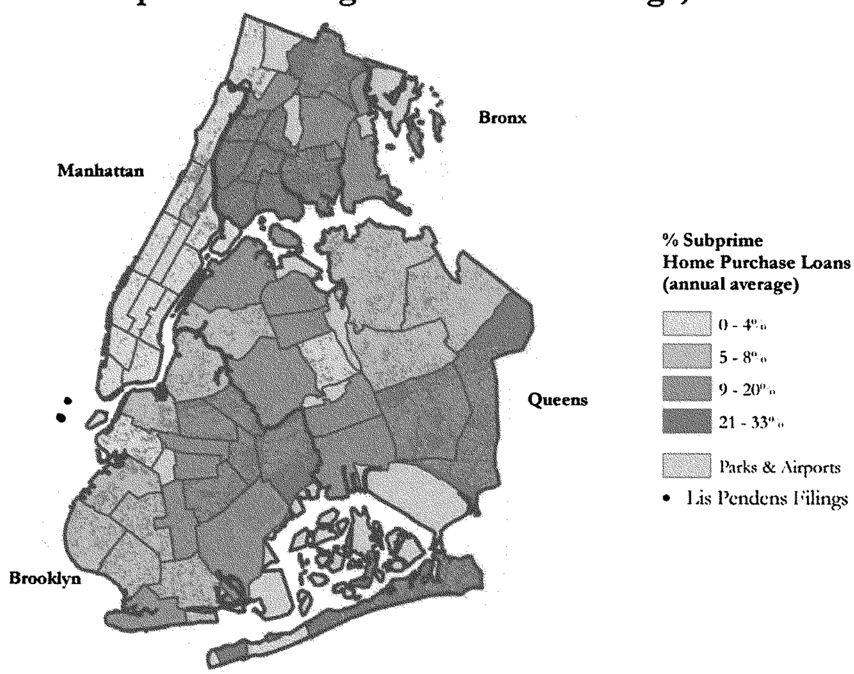
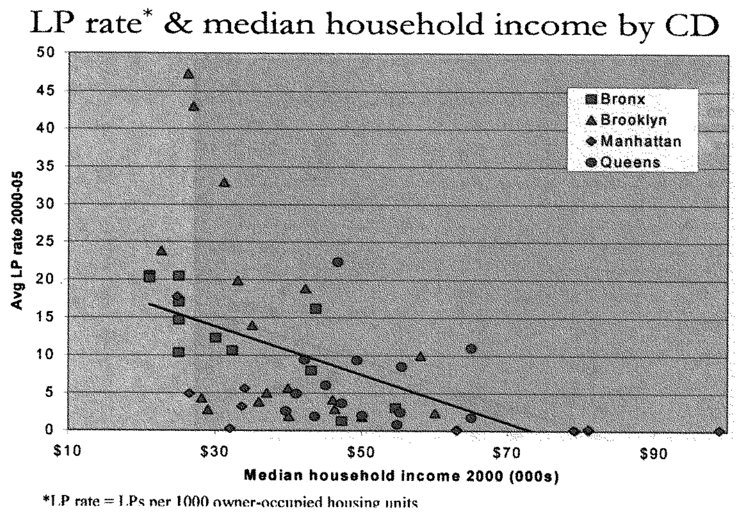
Figure 1

Subprime Lending & Lis Penden Filings, 2000-2005



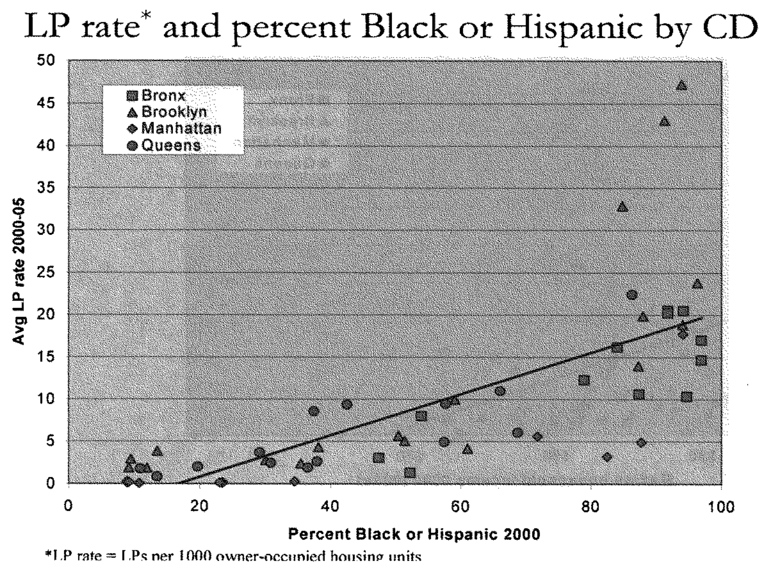
Source: Furman Center calculations of data from PDC and HMDA

Figure 2



Source: Furman Center calculations of data from PDC and the U.S. Census

Figure3



Source: Furman Center calculations of data from PDC and the U.S. Census

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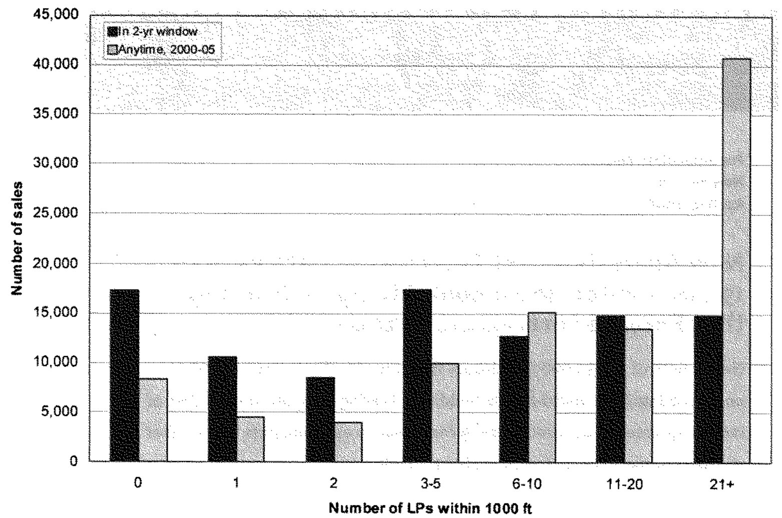
Figure 4: Distribution of sales by number of LPs within 1000 feet



Source: Furman Center calculations of data from PDC and NYC Department of Finance

APPENDIX C: Analysis of Renters Affected by Foreclosures

FURMAN CENTER FOR REAL ESTATE & URBAN POLICY
NEW YORK UNIVERSITY SCHOOL OF LAW ▪ WAGNER SCHOOL OF PUBLIC SERVICE
40 Washington Square South, Suite 314, New York, NY 10012 ▪ Tel: (212) 998 6713 ▪ http://furmancenter.nyu.edu

For Immediate Release
New York, NY
April 14, 2008

New Analysis of NYC Foreclosure Data Reveals 15,000 Renter Households Living in Buildings that Entered Foreclosure in 2007

Nearly 60% of the 15,000 foreclosure filings in New York City in 2007 were on 2 to 4 family or multi-family buildings, leaving a significant number of renters threatened by foreclosure. A conservative estimate puts the number of renter households impacted at about 15,000.

A new analysis by NYU's Furman Center for Real Estate and Urban Policy finds that a majority of the nearly 15,000 mortgage-related foreclosure filings in New York City in 2007 were on multi-family buildings, and only about 40% were on condominiums or single-family homes. The analysis shows that over 30,000 households (or about 76,000 New Yorkers) are living in properties that entered the foreclosure process in 2007. The Center estimates that more than 15,000 of these households (or some 38,000 New Yorkers) were living in rental units. This is a conservative estimate, because the analysis assumes that an owner lives in one of the units in all 2-4 family buildings, but in all likelihood, some of those buildings are completely occupied by renters.

Most tenants living in buildings going through foreclosure face eviction if the property is sold at auction. However, tenants protected by New York State's rent regulation laws, which apply to many units in larger 6+ buildings, are not at risk.

In 2007, New York City had approximately 15,000 foreclosure filings:

- 40% were on condo & single-family buildings
- 60% were on 2–4 family and 5+ buildings

More than 30,000 households are living in properties in foreclosure:

- 15,000 renter households
- 15,000 owner households

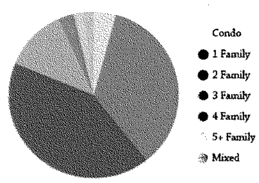
"It is not known how many buildings that entered foreclosure in 2007 will end up at auction, but the number of rental households at risk is troubling. The plight of renters in foreclosed buildings has not been part of the national conversation," said Vicki Been, director of the Furman Center. "Proposed

legislative reactions to the foreclosure crisis have focused on owner-occupants living in single-family homes, but the data reveal that, at least in New York City, there are many renters at risk. We need to craft responses that meet the needs of all those affected."

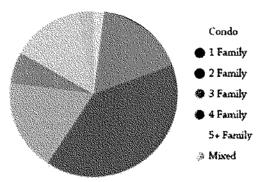
Nearly 11,000 of the 15,000 renter households living in buildings that entered foreclosure in 2007 reside in Brooklyn and Queens, with Brooklyn home to the largest share—about 7,200. Two community districts in Brooklyn, Bedford Stuyvesant and East New York, are each home to more than 1,000 renter households facing foreclosure.

"The recent scale of foreclosure filings is staggering," commented Ingrid Gould Ellen, co-director of the Furman Center. "Citywide foreclosures doubled between 2004 and 2007, with the highest rates of increase seen in 2 and 3 family buildings. If foreclosed multi-family properties are being bought by speculators, reverting to banks, or sitting vacant, we may lose a significant share of our stock of decent, affordable rentals."

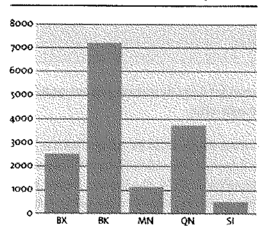
Breakdown of Properties that Entered Foreclosure in 2007



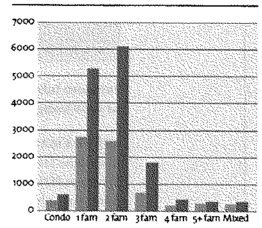
Breakdown of Total Units in Properties that Entered Foreclosure in 2007



Renter Households Living in Buildings that Entered Foreclosure in 2007



Foreclosure Filings by Building Type, 2004–2007 2004 2007



20 Community Districts with the Most Households Living in Buildings that Entered Foreclosure in 2007

Rank	CD Name	Borough	Total Households Facing Foreclosure	Renter Households in Buildings in Foreclosure
1	Jamaica/Hollis	Queens	2,852	919
2	Bedford Stuyvesant	Brooklyn	2,411	1,511
3	East New York/Starrett City	Brooklyn	2,107	1,155
4	Queens Village	Queens	1,517	395
5	Flatlands/Canarsie	Brooklyn	1,342	538
6	Bushwick	Brooklyn	1,269	820
7	East Flatbush	Brooklyn	1,187	596
8	Williamsbridge/Baychester	Bronx	1,043	488
9	Parkchester/Soundview	Bronx	1,025	708
10	Kew Gardens/Woodhaven	Queens	1,009	434
11	Brownsville	Brooklyn	962	580
12	St. George/Stapleton	Staten Island	931	308
13	Rockaway/Broad Channel	Queens	922	453
14	S. Ozone Park/Howard Beach	Queens	899	294
15	Crown Heights	Brooklyn	812	529
16	Jackson Heights	Queens	694	319
17	Washington Heights/Inwood	Manhattan	607	594
18	Tottenville/Great Kills	Staten Island	480	90
19	South Crown Heights/Prospect	Brooklyn	423	206
20	Ridgewood/Maspeth	Queens	418	234
Borough Totals				
1	Brooklyn		12,795	7,175
2	Queens		9,933	3,723
3	Bronx		4,188	2,483
4	Staten Island		1,785	488
5	Manhattan		1,334	1,111
New York City Total			30,035	14,980

For more information, contact Amy Armstrong at 212-998-6697, or armstrong@juris.law.nyu.edu.

THE FURMAN CENTER FOR REAL ESTATE AND URBAN POLICY is a joint initiative of the New York University School of Law and the Robert F Wagner Graduate School of Public Service at NYU. Since its founding in 1995, the Furman Center has become the leading academic research center in New York City devoted to the public policy aspects of land use, real estate, and housing development. The Furman Center is dedicated to providing objective academic and empirical research on the legal and public policy issues involving land use, real estate, housing and urban affairs in the United States, with a particular focus on New York City More information about the Furman Center can be found at http://furmancenter.nyu.edu.

Mr. KUCINICH. Thank you for that very significant quantification. Appreciate it.

Ms. Betts, please proceed.

Ms. BETTS. Yes. Thank you, Mr. Chairman.

Mr. KUCINICH. Can you get a little bit closer to that mic?

And, staff, could you make sure that mic is on.

STATEMENT OF PHYLLIS G. BETTS

Ms. BETTS. Thank you, Mr. Chairman, members of the committee.

I'm coming from Memphis, TN. We're not New York City. We're not southern California, Buffalo, Cleveland or Baltimore. To begin my message, I want to say that all of our markets are different.

House bill 5818 is a good bill, because it allows for that flexibility. It may not be veto-proof. If it's not, we need something similar.

And I want to share with you a little bit of our data from Memphis to underscore the need for flexibility and also for a funding formula that takes into account flexibility for market to market.

I'll speak to two points. Everyone has underscored and I think knows in their gut that the impact of foreclosures on neighborhoods is debilitating. I'm going to show some examples. Second, the data that we use to underscore a funding formula in terms of what will go to States and how States will distribute money within the States needs to be equitable in terms of regions of the country, different kinds of cities, different kinds of housing markets.

And I want to say just a couple of words about the apparent data base of choice, First American, and I think that my colleague, Mr. Talmage, will followup on that.

The debilitating impact of foreclosure, to point one. We're one of those areas of the country that didn't just get hit. Our foreclosure rate has been going up slowly since 2000. In 2007, we had almost 12,000 foreclosure notifications for a total in that 8-year period of over 61,000 foreclosure notifications. This is the equivalent of 25 percent of our single housing stock, our single-family housing stock, and that's where we are hardest hit.

Mr. KUCINICH. Excuse me, what was that percent again?

Ms. BETTS. Twenty-five percent of our single-family housing stock.

Mr. KUCINICH. Thank you.

Ms. BETTS. Our subprime lending escalated between 2004 and 2005, going up from 25 percent to 40 percent of all mortgage loans in Shelby County, and that includes our suburban area. And clearly, we're tracking subprime and foreclosures. And the neighborhoods that are hardest hit are hit both by subprime lending and by foreclosures.

Our hardest hit areas actually are those areas that we would call middle class neighborhoods; middle class neighborhoods with modest priced housing, where people moving from lower income neighborhoods are looking for a higher quality of life. These are the neighborhoods that are the most heavily impacted, that are going to have the greatest impact on our tax base in Memphis and Shelby County, and where this kind of intervention can make a difference. If we take a triage approach, this kind of bill can make a big difference in Memphis neighborhoods.

I would like to put up map two, please, which is the other map. The one on the bottom.

And if you could zoom in.

This is Memphis and Shelby County. I'm sometimes asked from folks in the northeast if that's the Mississippi River, and so I'm going to say, yes, that is, on the left of the map. Our downtown and center city area is right there on the river.

And then radiating north from the river is north Memphis, south is south Memphis. Those are our traditional low income areas. Most of our foreclosure there is driven by high cost refinance loans, often times second-generation folks who are taking out equity when parents die. And that's a different kind of situation that will require a different kind of remedy than what we are seeing in what we call the areas of the horseshoe.

You can see the darker the teal is where our greater number of foreclosures are. And in the north arc and the south arc in that horseshoe, foreclosure driven by subprime lending, which we can document, is moving out to our suburban area, in fact. If you see the lighter teal color, that is a suburban area. That is a different animal, but it is foreclosures none the less and requires the kind of intervention that you're talking about.

We're doing a neighbor-by-neighborhood survey and problem property audit, and that will be the next map. We're looking at the conditions of foreclosed properties and all of the other properties in the neighborhood for comparison purposes. And it has become quite clear that foreclosures are driving blight in these middle class—and by middle class, we're talking about $120,000 houses, which are actually quite nice in Memphis. So, you know, this is a different market. And if markets go, then so go Memphis and Shelby County.

This is Mendenhall Estates. In Mendenhall Estates, in 2007, the red parcels are the foreclosed parcels in Mendenhall Estates; 1,000 parcels, all single family, in this particular neighborhood; 65 foreclosed parcels, 6.5 percent of the single family housing stock. Fifteen percent of them were vacant when we surveyed them in the last month. And in the neighborhood as a whole, the other crosshatched parcels are showing signs of neglect.

When we drilled down to look at other vacant properties in this neighborhood, we found, for the 22 that we looked at that were in the worse shape, they were virtually all foreclosures from 2005 and 2006. Some of them had moved into the investor market. Others had been vacant the whole time.

Neighborhood stabilization, a public problem. Foreclosure mitigation, a private trouble. If the two are combined, we can begin to move forward.

Just a final note on the First American CoreLogic data base. When we have compared what is in that data base, which, according to its own documentation, covers about 50 percent of the subprime mortgages nationally, when we've compared the number of mortgages by zip code from that data base with the Home Mortgage Disclosure Act subprime mortgages, we're finding that in these heavily hit neighborhoods, only about 25 percent of the mortgages seem to be in the First American data base. Our theory on that is that these are modest mortgages, modest neighborhoods,

and they don't appeal as much to investors in terms of some of these securities instruments.

John will be looking at that. And if there's a difference of say 5, 7, 10 percent, if we compare Memphis and Tennessee to California or New York City, that's going to result in a major flaw in the funding formula. We want to have to deal with that flaw. That is we want this bill. We want this bill to be implemented.

In conclusion, thanks for the opportunity to contribute to this discussion, and I want to say that our neighborhoods in Memphis, TN, depend on it.

And I'm going to speak for New York City, I think the same is there as well.

Thank you.

[The prepared statement of Ms. Betts follows:]

THE UNIVERSITY OF
MEMPHIS

SCHOOL OF URBAN AFFAIRS & PUBLIC POLICY

600 JEFFERSON AVENUE, SUITE 453
MEMPHIS, TN 38105

Center for Community-Building
And Neighborhood Action

Testimony submitted by Dr. Phyllis Betts, Director
Center for Community Building and Neighborhood Action
pbetts@memphis.edu 901-678-1187

Chairman Kucinich, members of the Subcommittee, I very much appreciate the opportunity to testify on issues raised by HR 5818: The Neighborhood Stabilization Act of 2008. My name is Phyllis Betts, and I am the Director of the Center for Community Building and Neighborhood Action (CBANA) in the School of Urban Affairs and Public Policy at the University of Memphis in Tennessee. CBANA's mission is to "link research with action" on behalf of neighborhoods and quality of life issues associated with socioeconomic disparities. Our research on foreclosure has been supported in part by a grant from The Brookings Institution Urban Markets Initiative; we also work closely with The Urban Institute's National Neighborhood Indicators Partnership, where the emphasis is on using local data to better understand local context and drive policy in areas that include housing and foreclosure. Locally, our work is supported by the Community Development Council of Greater Memphis, the City of Memphis, and Shelby County government.

First, we in Memphis that are working on foreclosure and its impact on both families and neighborhoods appreciate the House's understanding that foreclosure is more than a private trouble. The debilitating effect on neighborhoods is a public issue requiring proactive public policy, and HR 5818 speaks to that understanding. It is a good bill that can be strengthened, and I hope that my testimony is useful in that regard. **My testimony this afternoon speaks to two points:**

1) The debilitating impact of foreclosures on neighborhoods and indeed, the fiscal health of cities -- is very real; HR 5818 is critical to enabling cities to intervene and stabilize neighborhoods. Using local data from public records on foreclosures and systematic observation data from our Neighborhood Survey and Problem Properties Audit, we illustrate how foreclosures drive vacancies and blight in high foreclosure neighborhoods in Memphis. Our data also underscores the relationship, which this committee well understands, between subprime lending and foreclosure.

2) Secondly, the data that Congress and HUD use to determine areas of highest impact and drive the funding formula for HR 5818 should not be biased to favor some states, cities, and local housing markets over others. In this respect, the apparent data source of choice -- First American CoreLogic Loan Performance -- is flawed. My testimony demonstrates a systematic bias against low and moderate income housing markets and in cities outside of the hottest and highest priced markets. It appears that subprime mortgage loans from low and moderate income and more moderately priced markets are less likely to be securitized by the private sector mortgage backed securities captured by First American. This means that First American understates the number subprime loans, delinquencies, foreclosures, and Real Estate Owned properties in low-moderate income markets compared to higher income and hotter markets.

1. The Debilitating Impact of Foreclosures on Neighborhoods: Illustrations from Memphis and Shelby County, Tennessee. Memphis and Shelby County are among those urban areas where foreclosure trends were well-established prior to what is being described as the 2007 "mortgage meltdown" and foreclosure crisis. From 2000 (when we began tracking subprime lending and foreclosures) through 2007:

- ☐ 61,590 Shelby County households have been served notice of foreclosure, equivalent to 25% of the single family residential housing stock.
- ☐ 11,623 foreclosure notifications were served in 2007 alone, involving 4.7% of single family households.
- ☐ Annual foreclosure notifications increased 152% from 2000 to 2007.
- ☐ Foreclosures are driven by high rates of subprime lending, which escalated from 25% to 40% of all mortgage loans in from 2004 to 2005.
- ☐ Over 40,000 subprime loans were made in Shelby County during the peak 2004 through 2006, with one of three Shelby County zipcodes having subprime lending rates (compared to prime loans) of at least 50% ; for the city of Memphis, subprime lending tops 40% in one of two zipcodes.
- ☐ Modest but erstwhile desirable moderate income neighborhoods have been hit hardest; evidence suggests that predatory mortgage brokers targeted lower income buyers only marginally prepared for the costs of home ownership in those neighborhoods. African American buyers appear to have been target-marketed.

Table 1 below documents the growing number of foreclosures zipcode by zipcode and distinguishes suburban zipcodes from Memphis City.

Maps 1 and 2 below illustrates how neighborhoods at all price points have been effected, with buyers in higher priced, more upscale suburban neighborhoods (on the right hand perimeter of the map) "pushing the envelope" with teaser and adjustable rates that stretched their capacity for successful home ownership. (The darker the teal color, the greater the number of foreclosures.)

Table 1

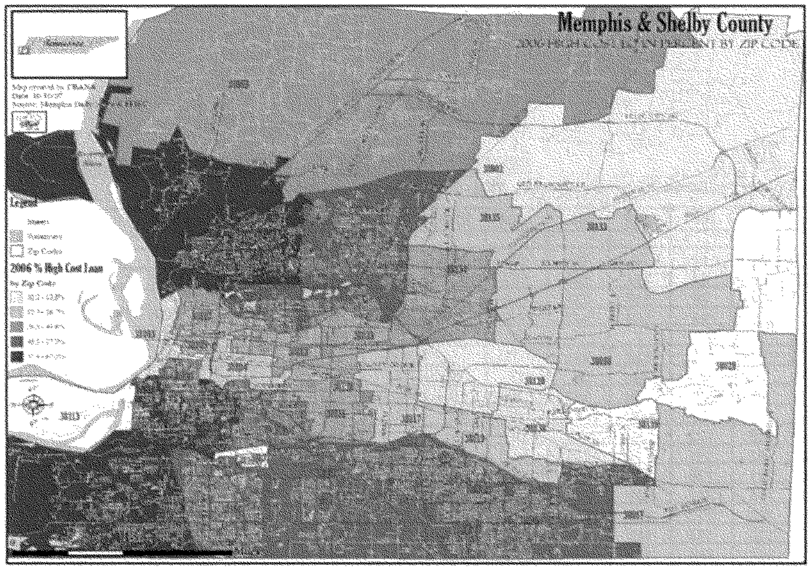
Shelby County Published Foreclosure Notices 2000 - 2007 *Source: Memphis Daily News*

Year	2000	2001	2002	2003	2004	2005	2006	2007	07 Final Sbtrust Deed	Total 00:07 Notices	% INCRS 00:07	% Final 07
38002	20	48	74	69	98	102	196	230	109	837	1050%	47%
38016	52	82	104	149	153	201	305	230	280	1276	342%	122%
38017	59	88	115	123	139	136	212	215	193	1087	264%	90%
38018	59	93	140	147	202	234	346	413	172	1634	600%	42%
38028	2	5	7	11	10	12	11	18	10	76	800%	56%
38053	63	82	114	134	133	150	153	192	83	1021	205%	43%
38103	14	9	19	21	23	22	30	41	15	179	193%	37%
38104	80	85	106	124	108	119	125	167	82	914	109%	49%
38105	24	26	33	43	30	41	39	38	28	274	58%	74%
38106	235	272	357	366	373	453	509	509	327	3074	117%	64%
38107	152	151	191	246	221	218	292	294	193	1765	93%	66%
38108	191	176	231	265	235	259	317	293	234	1967	53%	80%
38109	385	392	501	603	625	654	829	898	497	4887	133%	55%
38111	283	319	386	397	449	391	469	485	300	3179	71%	62%
38112	125	125	150	158	164	154	192	212	140	1280	70%	66%
38114	206	238	297	347	272	352	433	466	259	2611	126%	56%
38115	292	260	310	322	364	385	548	632	352	3113	116%	56%
38116	256	226	360	371	396	430	541	577	233	3157	125%	40%
38117	65	88	127	116	111	136	147	168	73	958	158%	43%
38118	337	329	462	488	499	529	710	752	385	4106	123%	51%
38119	39	45	53	67	84	102	134	134	60	658	244%	45%
38120	26	26	37	33	26	29	32	39	11	248	50%	28%
38122	156	186	230	245	245	260	303	300	189	1925	92%	63%
38125	138	199	258	318	381	477	576	827	358	3174	499%	43%
38126	30	39	32	33	24	33	39	39	18	269	30%	46%
38127	452	449	563	691	714	731	969	969	601	5538	114%	62%
38128	310	342	459	463	494	529	669	868	463	4134	180%	53%
38133	69	82	128	129	113	151	144	201	102	1017	191%	51%
38134	105	129	171	191	233	216	307	358	155	1710	241%	43%
38135	73	75	132	118	148	183	240	254	129	1223	248%	51%
38138	27	48	61	69	84	63	67	53	17	472	96%	32%
38139	13	17	29	18	36	28	39	47	14	227	262%	30%
38141	271	310	435	403	428	457	592	704	372	3600	160%	53%
TOTALS	4609	5041	6672	7278	7615	8237	10515	11623	6454	61590	152%	56%

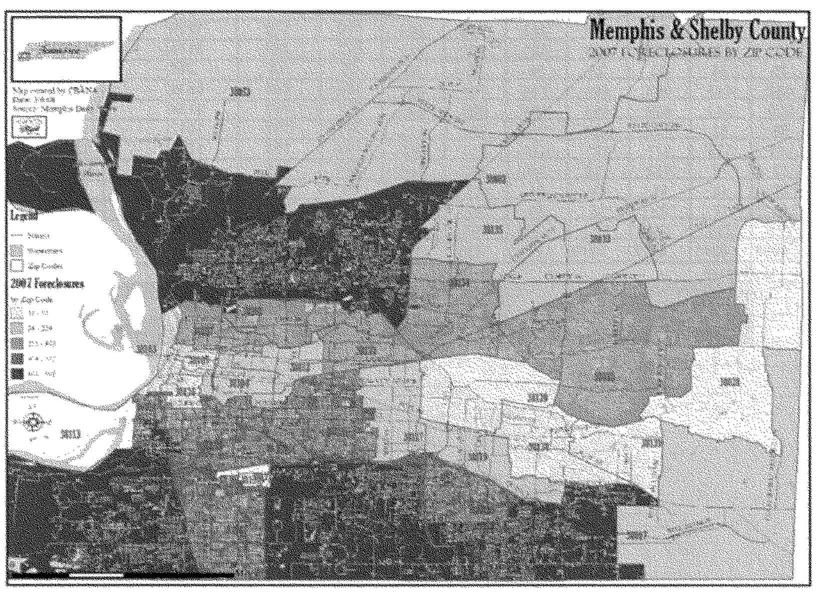
Legend	
Lakeland/Arlington	Millington
Partial Memphis/Cordova - County	Memphis City
Collierville	Bartlett
Eads/Fisherville	Germantown

3/06/08 AF

Map 1: 2006 High-Cost (Subprime) Loans by Zipcode



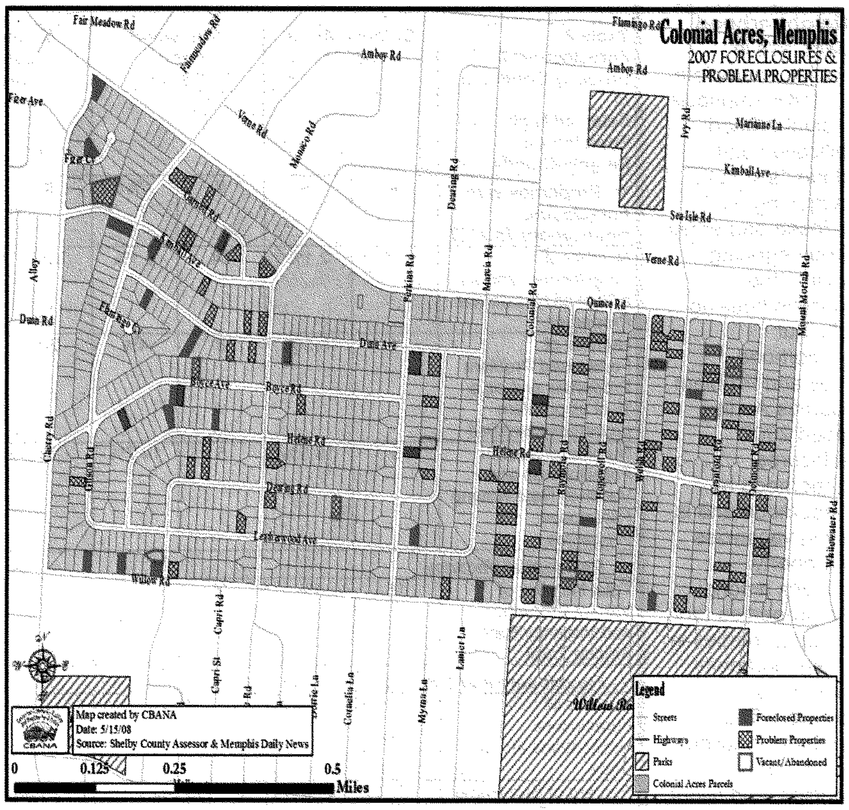
Map 2: 2007 Foreclosures by Zipcode

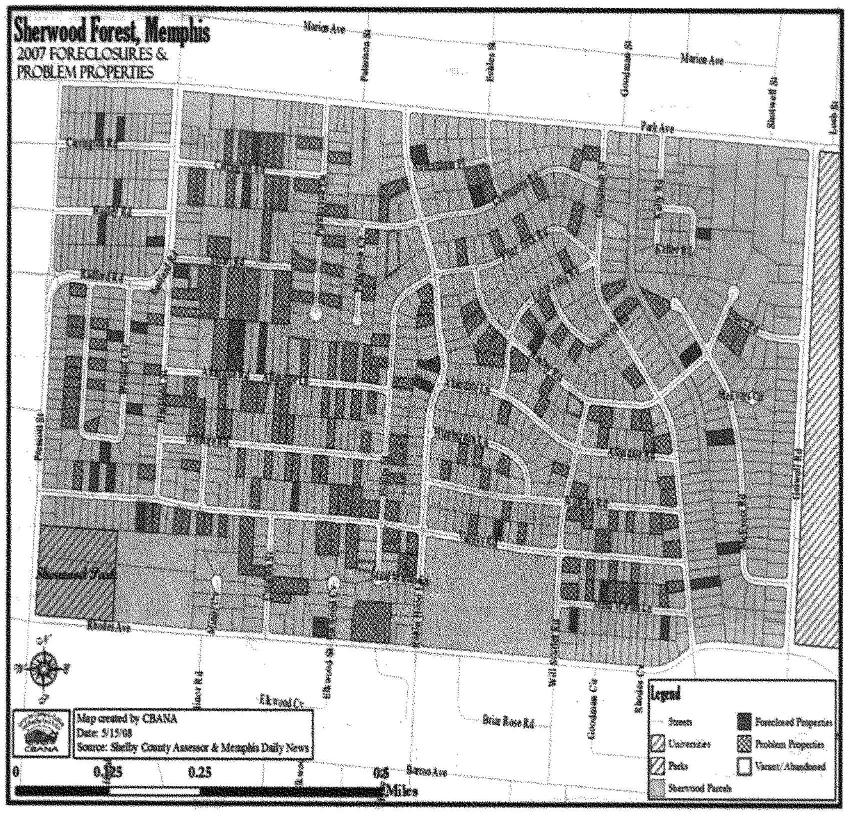


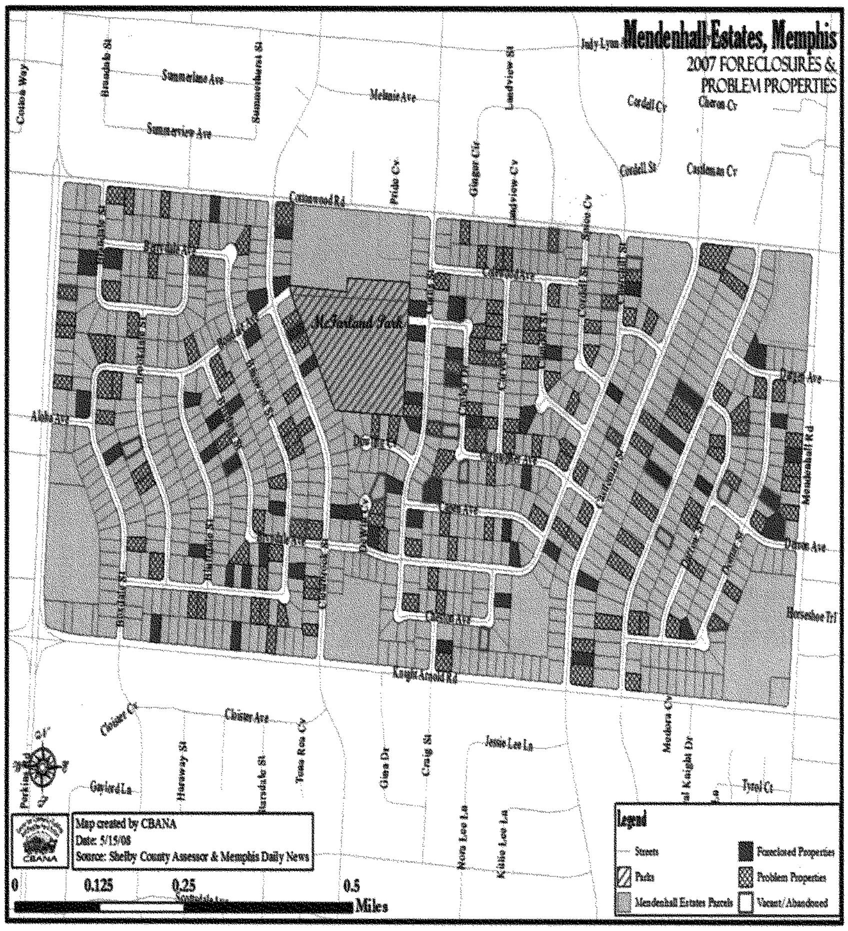
1. The Significance of Neighborhood Impact. We in Memphis appreciate HR 5818's emphasis on neighborhood stabilization and applaud its support for acquiring foreclosed properties and reintegrating them into the productive housing stock. Our Neighborhood Survey and Problem Properties Audit mapped 2007 foreclosures neighborhood by neighborhood and is auditing vaçancies and property conditions among those properties (and all other properties in the neighborhoods for comparison purposes.) The relationship between foreclosure, vacancies, and blight for three recently surveyed neighborhoods is summarized in Table 2 alongside, then illustrated by maps on the next pages. Colonial Acres, Sherwood Forrest, and Mendenhall Estates are three moderate income and modestly priced neighborhoods. In Colonial Acres, with a relative low 20% rate of subprime lending for 2006 and a very high rate of homeownership, foreclosures are fewer and are the ***leading edge for vacancies and blight***; In Sherwood Forrest and Mendenhall Estates, where subprime lending and escalating foreclosures took root earlier, and much of the property has already moved to the rental market, blight is more serious. We expect that "Vacant and abandoned" properties on the neighborhood maps are traceable to foreclosures in 2006 and 2005, and are in the process of integrating data from earlier years into our database; some foreclosures for 2007 are already currently vacant (red framed in yellow) or have become problem properties in other ways (red with cross-hatching.)

Table 2: Foreclosures & Property Condition in Selected High Foreclosure Neighborhoods	***Colonial Acres 38117***		***Sherwood Forest 38111***		***Mendenhall Estates 38118***	
√ ***Properties with Foreclosure Notifications in 2007***	#	%	#	%	#	%
Number of Foreclosures and as a % of all Residential Properties	27	2.1%	34	3.1%	65	6.5%
Number of Foreclosed Problem Properties and as a % of all problem properties identified	4	3.3%	8	4%	20	7.2%
Number of Vacant Foreclosures and Vacancy Rate Among Foreclosed Properties	5	18.5%	5	14.7%	10	15.4%
√ ***Residential Vacancy***						
Total Number of Vacant Properties and Vacancy Rate Among Total	15	1%	74	7%	31	3%
√ ***Foreclosure and Lending***						
Number of Foreclosure Notifications in Zip Code	171		490		753	
Percent of Sub-Prime Loans in 2006 in Zip Code	20.5%		33.8%		55.1%	
√ ***Overall Condition of Housing Stock***						
Number and percent of all single family homes identified as problem properties	120	11%	198	18%	277	28%
Total Number of Single Family Homes	1,115		1,109		1,002	

Memphis 2007 Foreclosure Notifications from "Neighborhood-by-Neighbor: A City-Wide Problem Property Audit," 1st Qtr 2008. Mortgage lending data from HMDA dataset, 2006
©Center for Community Building and Neighborhood Action University of Memphis


Colonial Acres, Memphis
2007 FORECLOSURES &
PROBLEM PROPERTIES
Fair Meadow Rd
Amboy Rd
Flamingo Rd
Verne Rd
Monaco Rd
Dearing Rd
Marianne La
Kimball Ave
Sea Isle Rd
Perkins Rd
Marvin Rd
Colonial Rd
Quince Rd
Mount Moriah Rd
Dunn Rd
Dunn Ave
Boyce Rd
Helene Rd
Leatherwood Ave
Willow Rd
Capri Rd
Capri St
Cornelia La
Myrna La
Lanier La
Whitewater Rd
Map created by CBANA
Date: 5/15/08
Source: Shelby County Assessor & Memphis Daily News
0
0.125
0.25
0.5
Miles
Legend
Streets
Highways
Parks
Colonial Acres Parcels
Foreclosed Properties
Problem Properties
Vacant/Abandoned


Sherwood Forest, Memphis
2007 FORECLOSURES & PROBLEM PROPERTIES
Marion Ave
Patterson St
Echles St
Goodman St
Marion Ave
Sherwood St
Park Ave
Loeb St
Sherwood Park
Rhodes Ave
Prescott St
Ekwood Cv
Elkwood St
Briar Rose Rd
Will Shelter Rd
Goodman Cv
Rhodes Cv
Baron Ave
Map created by CBANA
Date: 5/15/08
Source: Shelby County Assessor & Memphis Daily News
CBANA
0
0.125
0.25
0.5
Miles
Legend
Streets
Universities
Parks
Sherwood Parcels
Foreclosed Properties
Problem Properties
Vacant/Abandoned


Mendenhall Estates, Memphis
2007 FORECLOSURES & PROBLEM PROPERTIES
Map created by CBANA
Date: 5/15/08
Source: Shelby County Assessor & Memphis Daily News
0
0.125
0.25
0.5
Miles
Legend
Streets
Parks
Mendenhall Estates Parcels
Foreclosed Properties
Problem Properties
Vacant/Abandoned

2. The Funding Formula and Bias in the First American CoreLogic Database.

The "Foreclosure Shares" funding formula for states as set out by Section 5(d) of HR 5818 is based on number of foreclosures and number of subprime loans at least ninety days delinquent. States' loan and grant allocations from the total appropriation will equal *their proportionate share of the total number of foreclosures and ninety day delinquent subprime loans* documented for the nation as a whole. The database used to capture these numbers should 1) be equally likely to include subprime loans and delinquencies from weaker and more modestly priced housing markets as from hot and higher priced housing markets; 2) draw proportionately from different regions of the country and from different size cities; and 3) not discriminate based on borrower characteristics such as race and ethnicity. We know that First American CoreLogic Loan Performance database – the apparent database of choice for formula-driven allocations – includes only about 50% of subprime loans nationally. This would be acceptable if every housing market were equally likely to be included in that 50%. Our data from Memphis and Shelby County suggests that this is not the case. For example, comparing the number of subprime loans reported to the Home Mortgage Disclosure Act (HMDA) for 2006 with First American subprime loans originated in 2006, we find that only about 45% of HMDA loans appear to be represented. This means that some other areas have to be over-represented to make up for Shelby County's under-representation. A difference of 5% is a big difference at the numbers of loans that are in play.

More troubling, the most dramatic gaps between HMDA numbers and First American numbers are in low and moderate income neighborhoods with the greatest number and proportion of delinquencies and foreclosures: *in Memphis' highest foreclosure neighborhoods,* ***only about 25% of loans*** *appear to be represented in First American.* This means that weak market cities like Cleveland, Detroit, Buffalo, and other mostly medium-sized cities that tend to be in the northeast-midwest corridor are even more disadvantaged than Memphis, which is only "on the border" of being a weak market. *These cities are likely to have* ***as much as 75% of their loans*** *excluded by the First American database.* A plausible explanation is that subprime mortgage loans from low and moderate income and more moderately priced markets are less likely to be securitized by the private sector mortgage backed securities captured by First American. Funding formulas based on this kind of bias in the database are fatally flawed and should be amended as the Neighborhood Stabilization Act of 2008 is implemented.

We also recommend that the funding formula be amended to take into account another source of diversity in housing markets. HR 5818 already includes an adjustment on loan dollars for the cost of property acquisition in higher priced markets. There is, however, no adjustment for the higher proportionate cost of rehabilitating housing in weaker and lower-priced markets; in many Memphis neighborhoods hit hard by foreclosure, rehabilitation subsidies will be required since the cost of acquisition and rehabilitation will exceed market price for resale. While HR 5818 allows that grant funds may be used for rehabilitation, unlike the adjustment for the cost for housing acquisition in high-priced hot markets, there is no adjustment in the formula to take *these* market-driven requirements for subsidy into account in lower-priced and weaker markets. Subsidies are essential to neighborhood stabilization in these markets and should be taken into account as a formula adjustment; for example, the adjustment could be triggered by data showing relatively low market values and outstanding loan amounts that are close to or exceed market values. While "upside-down" loans are going to be found in all markets (where the outstanding loan amount exceeds current market value), the challenge for rehabilitation is greatest in those markets where the need for rehabilitation is greater (most likely the case in

lower cost markets) and where the cost will be disproportionately large compared to likely resale dollars generated.

In conclusion, HR 5818 is a strong step in the right direction: it recognizes that the neighborhood impact of the foreclosure meltdown takes the form of a ripple effect going beyond the private troubles of foreclosed families; that foreclosure-driven blight will not be reversed by a "market correction;" that foreclosure-driven blight is a public issue requiring pubic policy interventions. We in Memphis and Shelby County Tennessee urge veto-proof support for HR 5818 and revision of the funding formula by which the Neighborhood Stabilization Act of 2008 – or such bills as may result from House and Senate reconciliation – makes funding available to neighborhoods in need across the country.

Mr. KUCINICH. I thank the gentlelady.

Mr. Talmage, please continue with your testimony.

STATEMENT OF JOHN TALMAGE

Mr. TALMAGE. Thank you, Mr. Chairman, and thank you for inviting me to participate in this hearing because I think what it does——

Mr. KUCINICH. Would you please bring that mic up a little bit closer, so that we can all hear you clearly?

Mr. CUMMINGS. Is it on?

Mr. TALMAGE. There we go. How about that?

Thank you for inviting me because I think this highlights the problems that we have with understanding economic conditions in inner city neighborhoods in the United States, that our own work at Social Compact has found that in your own city of Cleveland, when we worked there in 2002, we found 100,000 people not counted by the U.S. Census that lived in Cleveland. In African-American neighborhoods in Miami, we're finding 95 percent higher populations than have been documented by the U.S. Census.

And I think there is very little attention or understanding of the market conditions of inner city America. This has impacts at the household level as well as the neighborhood level. In recent work in Harlem, we found that 40 percent of addresses don't have credit scores associated with them. In the city of San Francisco, 33 percent don't. And so this lack or absence—or this lack of information has created risk adversity in the commercial lending sector but risk exuberance in the residential lending sector, but it is based on the same lack of documented information about communities.

And I just have to say before I talk about the foreclosure issue that, while the scope of the hearing certainly appropriately focused on the impact of foreclosures, the scale of the problem extends, spills over to a broader community development challenge around retail. There is emerging evidence now that's beginning to correlate the correlations with obesity and diabetes rates and the lack of access to full service groceries. Those grocery stores are imperiled in underserved markets. There is a group of evidence that is beginning to emerge on the incidents of crime and the saturation of pawn shops and payday lenders and whatnot. And those numbers will continue to increase as our neighborhoods are imperiled.

So those same kind of conditions and these same kinds of challenges that we as a community, whether it is the Urban Institute or Social Compact or the NNIP Partnership, are all trying to face everyday are now imperiled because of the lack of understanding we have at the neighborhood level.

In our own work, we've had to create a tool that allows us to understand the foreclosure impact, because just this week, when we were out at the International Council of Shopping Centers with a variety of cities discussing this work with retailers, they were all interested in what is the foreclosure impact in Detroit or in Cleveland or whatnot. So the 15,000 stores that they may be closing this year and certainly not building will be drawn to these numbers as we begin to propagate them. But by depending on national data sets, we're not going to have the full understanding of what's going on in Fruitvale, Oakland, or South Central LA or places like that.

We've had—so because of this, we've had to create a response where we have partnered with a variety of private-sector partners such as Property Advisors out of Cincinnati, Ohio; First American CoreLogic; and University Partners to begin to build out our own tools so that we can now assess the market value of every home in the city of Detroit, the foreclosure value of that same home, the abandon value of that same home, the impact on adjacent properties, the impact on city taxes and whatnot, and do that in a real time meaning, because as the city of Detroit begins to address their own foreclosure issues with their own foreclosure office and whatnot, they have to have a dashboard to be able to understand what the impact of this problem is.

And just to sort of put this in perspective, when you look at the statistics that are being put out there about Wayne County, which Detroit is located in, where the Center for Responsible Lending estimates that the impact on every unit in Wayne County, there's been a $1,700 impact. The fact of the matter is, if you look at the foreclosure data itself it is a $15,000 impact. This is not on a $200,000 home; this is on a $60,000 home. So on the for—on average, the foreclosure impact has been almost 25 percent.

The market conditions for market rate housing, the 65,000 transactions that have been conducted in the last 2 years, has led to a depressed 10 percent impact across the board on every single home. So that, to the extent—to the point that the panel has made, that this is now spilling over greatly on the adjacent properties, on other parts of the market. And I think that, until we can create the tools that allow us to have the skill to understand what the—the individual impact is on households and on neighborhoods, that we can't create the level playing field. And I have to stress that, in our own work, having information to be a place where people, stakeholders can come together to understand what the existing conditions are, to agree at least on what that information is; it is inefficient to try to find lots of other solutions without having that common understanding of what neighborhood conditions are.

And so I think that the kind of tools that we're talking about, that Phyllis is talking about, that others are going to talk about creates the existing conditions that we can all agree on, and then we can build solutions from that.

Thank you, sir.

[The prepared statement of Mr. Talmage follows:]

Measuring Mortgage Foreclosure Impact: New Decision-Making Tools to Address the Foreclosure Challenge

Mr. John Talmage
The Social Compact, Inc.

Testimony before the House Committee on Oversight and Government Reform
Subcommittee on Domestic Policy
May 21, 2008

Mr. Chairman, and other members of the Committee, thank you for the invitation to testify today regarding the mortgage foreclosure challenge facing America's communities and how innovative information tools can guide investors and government decision-makers toward improved and appropriate interventions and inform public policy decisions that result in stronger, healthier neighborhoods in which to live and do business.

I would like to begin by making three points.

1. The community development field is increasingly looking toward asset-based initiatives in response to local economic challenges and opportunities. The current foreclosure challenge poses a significant threat to the assets of homeownership, occupancy and community wealth. The response to the foreclosure challenge should remain framed by the goal of preserving and stabilizing community assets whether through public or private interventions.

2. As large and complex as is the foreclosure challenge, any satisfactory response must depend on accurate and adequate information to support an approach enabling analysis and intervention at both the macro and micro scales.

3. Under the banner of an emerging new paradigm in community economic development called "information-led development," Social Compact and Property Advisors, supported by First American CoreLogic, have piloted a forward-looking, real-time tool leveraging a variety of public and proprietary data sources capable of measuring, projecting and prioritizing the impact of foreclosures in Detroit, MI which could serve as a model for assessing and responding to this challenge in other cities similarly affected by foreclosure.

Asset-based Initiatives: Solutions for Bridging the Information Gap on LMI communities

With the foreclosure challenge continuing to accelerate across the map, there is every indication that all socio-economic segments of America will be touched by this reality. Still, low and moderate-income (LMI) communities stand to shoulder the worst of the fallout, not only because they are disproportionately exposed, but also because they will be the least equipped to respond to the accompanying market pressures and follow-on impacts. Indeed, Federal Reserve Chairman Ben Bernanke noted as much in his September 2007 testimony before the House Committee on Financial Services: "The consequences of default may be severe for homeowners, who face the possibility of foreclosure, the loss of accumulated home equity, and reduced access to credit. In

addition, clusters of foreclosures can lead to declines in the values of nearby properties and do great damage to neighborhoods."[1]

This does not constitute news, but signals how the profound threat of the current foreclosure challenge could erase the hard-won neighborhood gains of community organizations and intermediaries. Such a setback for community economic development will ensure that a full understanding of the fundamentals of LMI communities will be yet further beyond our grasp.

Mr. Bernanke's testimony highlights the significance of the foreclosure challenge and underscores an important point: it is not only the defaulting homeowner who is impacted by foreclosure, but adjacent property owners and the community at large. Precisely because the foreclosure challenge will have serious repercussions even beyond housing that will further impede families' and communities' ability to weather the storm, I do not believe that a singular, simple solution exists or that such a one-size-fits-all solution will emerge. As financial institutions become increasingly risk-averse to recoup the substantial losses incurred by foreclosure fallout, we can expect diminished lending to start-up entrepreneurs and small businesses, further limiting the number of wealth creating opportunities in our neighborhoods. Concentrations of foreclosures will leave some communities with far fewer residents translating into smaller markets without the consumer density attractive to retailers and financial institutions. This has broader implications than just the investment climate; impacting some public policy goals now linked with private investment activity such as public health outcomes correlating increased rates of obesity and diabetes with limited access to full service grocery, or the relationship of incidents of crimes with the saturation of alternative financial services such as check-cashing and payday lending outlets.

With the existing shortage of timely and accurate information around socio-economic conditions in LMI communities already clouding their prospects from the perspective of public-policy makers and private sector investors, failure to properly understand the foreclosure challenge can only add greater uncertainty. In fact, the tightening credit markets are just such an indication, another barrier to capital access in these communities and continued expansion of the information gap as the number of transactions shrinks, limiting comparative measure.

Leading thinkers like Robert Weissbourd and Tom Kingsley have urged the community development field toward an understanding of how these serious information gaps compromise effective public policy and investment responses to the challenges and opportunities facing LMI communities. Firms such as Social Compact, LISC-MetroEdge, Urban Institute, and Initiative for a Competitive Inner City (ICIC) have been working to correct these information asymmetries in LMI communities through a series of asset-based approaches aimed at removing capital barriers to stimulate investment. In every instance the way forward has been lead by information innovations in concert with coordinated partnerships and framed by asset-based development strategies.

The tools and techniques emerging from this information-led development platform have produced compelling results at a micro level through combinations of public and proprietary data, enabling community successes and ensuring new opportunities for LMI neighborhood residents. Understanding that LMI communities are disproportionately affected by the foreclosure challenge, I would urge, in the rush to identify a tenable solution, a close examination of these effective

[1] Bernanke, Ben S. (Speaker). (2007). "Subprime Mortgage Lending and Mitigating Foreclosures." Washington, D.C.: Committee on Financial Services, U.S. House of Representatives.

methodologies, that we might harness an appropriate variety and depth of information rather than abandon these proven strategies for a concept too far in the offing to provide a solution desperately needed immediately.

This is not to say the solution to the foreclosure challenge already exists, but that ongoing efforts to understand and quantify it are beginning to bear fruit. These localized tools allow for nuanced approaches through the integration of varied, and alternative, data. Most importantly they can be made scalable.

Valuable datasets such as Home Mortgage Disclosure Act (HMDA) data and 2000 Census data, though standard and available in granular detail, are too dated on their own to accurately describe the velocity and impact of the foreclosure challenge to properly inform the forward-thinking, targeted decision-making that the response to the situation demands. We can ill-afford to base today's response on lending data describing trends two years old or hope to reasonably expect to assist communities based on their characteristics eight years ago given the dramatic changes experienced from the real estate boom of the last decade. Waiting for the 2010 Census estimates to become available is similarly unrealistic.

Developing Strategic and Decisive Responses to the Foreclosure Challenge

Through American Housing Rescue and Foreclosure Prevention Act, and the Neighborhood Stabilization Act, the House has begun to acknowledge the scale of the foreclosure challenge and initiated its first response. The Neighborhood Stabilization Act, in particular, is designed to help communities hit hardest by the housing foreclosure crisis. The Act proposes the authorization of a $15 billion federal grant and loan program to assist what many state and local governments are already beginning to do: purchase, rehabilitate, and resell or rent foreclosed homes.

The Bill has two primary objectives. As Congresswoman Waters states, firstly the Bill "targets assistance where it is most needed". Secondly the bill put funds "on the street" quickly enough to stimulate the economy." The National Foreclosure Prevention and Neighborhood Stabilization Task Force forecasts that the bill will generate at least $38 billion in direct and "ripple effect" economic activity nationwide, employ 120,000 people, and restore nearly $225 million per year in local government real estate tax collections. [2]

Only by ensuring that these measures are felt on the ground in impacted communities will this legislation be effective. There will be too many losers and too few winners as the mortgage foreclosure challenge evolves, but the well-timed application of better information utilizing the best of the public and private sectors' existing tools will help us minimize the damage that is occurring to our country's homeowners, their neighbors and all of our communities.

Without an accurate, granular, dynamic and interactive overview of local housing trends, resources are likely to be spread too thin across too large a landscape with modest results. While private sector

[2] House Committee on Financial Services Press Release, May 2008. (2008). "House Passes Bill Introduced by Congresswoman Waters to Help Communities Hit Hardest by Foreclosure Crisis"

redevelopment solutions are often available, they typically remain on the sidelines in the mire of neighborhood decline.

Foreclosure Impact Analysis Tool: Capturing Complexity, Delivering Clarity

Social Compact in partnership with Property Advisors, an Ohio-based real estate consultancy, and supported by First American CoreLogic, have piloted a foreclosure impact analysis tool in Detroit, MI that:

- captures the complexity of mortgage foreclosures and their impacts in communities, and;
- provides clarity for public officials, private investors and community intermediaries with limited resources and time, to take prompt and decisive action where the initial resources available can achieve the most positive impact.

Though piloted in Detroit, this tool, designed to assess neighborhood housing health, is constructed on a robust platform of scalable data, methodologies and communications that could examine any neighborhood in any major American city and determine, in collaboration with City leadership and community stakeholders, the most important neighborhoods to target for the deployment of City, State or Federal resources toward greater economic health.

As the dimensions of the foreclosure challenge become magnified, the real estate axiom "Location, location, location" holds true. Already, the Foreclosure Impact Analysis tool pilot demonstrates this in the early findings in Detroit. The Center for Responsible Lending, in an issue paper exploring foreclosure impact in the U.S. at a county level, concluded that housing units affected by foreclosure decreased home values by $5,000 on average across the country, and estimated impact in Wayne County, MI at about $1,700 per housing unit with the cumulative negative effect on Wayne County home values at $1.0 billion[3]. Early findings from the Foreclosure Impact Analysis tool in Detroit show the loss in value of foreclosed properties at an average of over $15,000 per unit and impacting total Detroit housing stock alone at nearly $1.0 billion, or roughly $3,000 per housing unit. Considering that Detroit housing stock accounts for about 40% of Wayne County housing stock[4], the implications of these early results highlight the need for tools to go beyond macro-level analysis.

As such, the approach behind the Foreclosure Impact Analysis tool begins with an understanding of metro-level trends to define and calibrate the underlying financial, services and entitlement forces that affect all neighborhoods. An ongoing analytic process, the tool is capable of revealing the trends and concentrations of market forces that forecast any neighborhood's current housing health and potential going forward. This relevant, communicative approach fosters neighborhood impact assessment, prioritizes necessary responses, and with appropriate resources in place, begins neighborhood healing. Perhaps most importantly, this approach allows the study and communication of any neighborhood's direction at the household level.

At the rooftop level, housing portrays the granular economy of any City, the household buying power, stability and depth of sustained wealth. Neighborhood housing health can be measured

[3] The Center For Responsible Lending. (2008). "Subprime Spillover: Foreclosures Cost Neighbors $202 Billion; 40.6 Million Homes Lose $5,000 on Average." Durham, North Carolina.
[4] According to the 2006 American Community Survey (ACS).

through thoughtful combination of recorded housing data, demographics, value trends and modeling. From this framework, we established the baselines and metric boundaries for a rich collection of historical and current property record data provided by First American CoreLogic assembled by pertinent housing data: neighborhood, transfers, tax values, absentee ownership, parcel number, property living area and year built, for example, for the most recent, completed three years. These housing data, integrated through analytical modeling and housing value filters, are then correlated with current Social Compact demographic estimates to organize a detailed scan of each neighborhood's housing outlook. Combined, these data unlock embedded markers that bolster neighborhood health, and those that signal its deterioration.

This Foreclosure Impact Analysis tool allows us to evaluate and reasonably predict three property value scenarios based on current market conditions: Market, Foreclosed, and Abandoned. Without bias, the model yields a "vitality score" for each block group, ranking neighborhoods from healthiest to those most threatened by deteriorating housing assets. Some of the metrics analyzed include: ARM counts, price volatility, distressed property discounts, ownership, arms-length "market" transfer counts, foreclosure counts, pre-foreclosure counts, median sale prices, tax assessment land valuations, household counts, and household incomes.

Through careful assemblage and tracking, precise trends of value, ownership and neighborhood stability can be seen, charted and analyzed. After filtering and sorting of the housing data, historical trend charts reveal comparative tracks of median sale prices for arms-length "market" transfers against median sale prices of foreclosed properties, demonstrating the relative price volatility for the same "market" sales against the same foreclosures. Price volatility is an index used to evaluate the consistency and stability of the market's valuation of properties. This allows for trending the sales price impact of foreclosure activity by tracking corresponding relative price discount against the "market" sales, and is capable of outlining real estate tax implications affecting the City depending on whether a home sells at a market or foreclosure sale price.

Census block group level analysis allows for the gauging of market values in a given geography. By comparing foreclosed property values to their prior market sale values and combing this data with the built in scorecard modeling, an estimated "Foreclosure Discount" percentage is calculated for the specified block group. This percentage represents the approximate loss in value as related to the distressed sale. Neighboring block groups may have Foreclosure Discounts that are very similar or drastically different, depending on the health of these neighborhoods.

Because home values are only as strong as other homes in the neighborhood, foreclosed properties have feedback effects that undermine the values of surrounding homes over some period of time. In determining the impact foreclosed homes have on neighboring homes, a similar methodology is applied to calculate an estimated "Market Discount" percentage for each block group. This represents the approximate loss in value as related to the value depression caused by neighboring foreclosed homes. Homes within healthy and established neighborhoods are better positioned to be resilient to the viral effects of neighboring foreclosures than homes in transitioning neighborhoods, sometimes resulting in a positive Market Discount percentage.

Information from the tool's Neighborhood Scorecard and Real Estate Tax Impact Table can be manipulated to test the outcomes and varying scenarios and displayed in a series of Hot Spot Maps. These maps allow community leaders and officials to readily prioritize the deployment of required resources. In addition, Hot Spot Maps allow for the analysis of the feedback effects from strongly

impacted communities into healthier areas.

This Foreclosure Impact Analysis tool is a richly textured analysis of public and proprietary data that weaves together the perspectives of multiple lending portfolios across varying geographies. Such a framework allows a broad community of users, from government leadership, lending institutions, community organizations, homeowners and housing advocates to determine appropriate paths to action through the ability to test the impacts of those action plans against other optional strategies.
I believe this scalable tool can serve as a model for targeting and tailoring appropriate solutions to the foreclosure challenge facing the nation, as well as other broad community development opportunities and concerns. Built on sound information and capable of exploring that data at metro, neighborhood, block group and household levels, it represents a powerful analytic capable of layering multiple lenses on top of a granular geography to define the extent and impact of foreclosure activity and explore the effect of potential interventions. The results from the ongoing Detroit pilot point to considerable utility in other markets where the foreclosure narrative continues to unfold.

The approach behind this tool allows for a broad group of stakeholders to work from a common platform to correct information asymmetries. The existence of these asymmetries introduces further inefficiencies to possible solutions, as well as the public discourse itself, by diluting the impact of both public and private resource investments. Perhaps more importantly, it will continue to foster divergent and unrealized expectations among all interested parties, undermining the good faith efforts of community, government and private sector led efforts to provide solutions. Information is a practical foundation with real potential to bring parties together. The long road to recovery has to begin from a common understanding of the scope of the problem, consensus on how to measure the impact and success of new initiatives and a renewed commitment to community development to operate in a public policy framework that supports the efforts of the public and private sectors working together to realize their own, but not mutually exclusive, goals – an appropriate return on private investment and effective community renewal.

The well-timed application of better information utilizing the best of the public and private sectors' existing tools will help us minimize the damage that is occurring to our country's homeowners, their neighbors and all of our communities. Let us connect the resources marshaled today to confront this challenge to effective, information-based strategies, public and private, to preserve and protect our community assets to guarantee tomorrow in all of our communities, for all of our residents.

Mr. KUCINICH. I thank the gentleman.

We're going to move to questions now to talk about the appropriateness of Federal intervention.

And Professor Been, you've stated that there is justification for intervening, I think you've said, directly to protect neighbors, tenants and communities. As you may know, however, there is opposition of Federal intervention on the grounds that intervening creates a moral hazard. In your opinion, does the specter of a moral hazard arise in a Federal intervention to help neighbors? And if it does, what are your thoughts about it?

Ms. BEEN. The problem of moral hazard——

Mr. KUCINICH. Could you bring—make sure that's on and bring it closer.

Ms. BEEN. Oh, I'm sorry.

The problem of moral hazard usually, you know, is considered to be this situation where a decisionmaker is able to escape the cost of some of their decisions and therefore may take riskier actions. Right?

The neighbors of these properties, the tenants of these properties and the community weren't involved in the decision whether or not to take out this loan or whether or not to grant this loan. Right? So they are suffering from external effects. They are suffering from costs that they had nothing to do with.

Now I'm not saying that moral hazard won't in some way affect the future decisions of those people. I mean, if a neighbor sees, you know, one of their neighbors being rescued in some sense, then they may make more risky decisions. But you're trying to balance here the problem of these external effects being imposed upon people who weren't part of the decision, which is the classic reason that we always support government intervention. Right? And you're trying to balance that very real need to protect those third parties who weren't part of the decision against, you know, the moral hazard that may be involved down the road——

Mr. KUCINICH. You said that——

Ms. BEEN [continuing]. Balancing test.

Mr. KUCINICH. You said that foreclosure-driven blight will not be reversed by a market correction, that foreclosure driven blight is a public issue requiring public policy interventions. As you know, the administration seems to be—strike that.

This is to Ms. Betts. You've said that, with respect to foreclosure-driven blight, that it requires public policy interventions. As you know the administration seems to be taking a different view for the moment. What, in your view, is the future of neighborhoods distressed by the subprime mortgage meltdown if they have only the market to correct their problems and no Federal intervention?

Ms. BETTS. I think one of the witnesses earlier was talking about how some properties can be reintegrated into the housing stock by the market. And typically those are going to be the more valuable properties.

I would like to connect that with the discussion here of moral hazard in that the brokerage system of independent mortgage brokers and independent mortgage companies, that part of a dysfunctional mortgage market was highly fraught with moral hazard. The absence of fiduciary responsibilities on the part of brokers with

their clients and so on, that form of market failure is in fact what put us where we are at this point in time, such that an intervention that can make a difference in neighborhoods that are on the cusp, an intervention that could help revitalize some neighborhoods that are closer to the precipice, an intervention that can make a difference in inner-ring suburbs. I think that the overall cost of this hasn't adequately been calculated by those who would say that this isn't a public policy issue.

Mr. KUCINICH. I want to go back to Professor Been.

You have found that the amount of decrease in housing values that can be attributed to the foreclosure of neighboring property values, according to the concentration of—varies according to the concentration of foreclosures. For the record will you explain to this subcommittee the difference between looking at the concentration of foreclosures on one hand versus the number of foreclosures on the other?

Ms. BEEN. Well, you have to really look at both, because obviously a neighborhood that's affected by tremendous concentration of foreclosures is destroyed. Right? I mean, it's very seriously impacted.

But in terms of figuring out the overall effect of foreclosures, you also have to look at the number of properties that are being affected. So think of it as, if you have 100 foreclosures all concentrated in one neighborhood versus 100 foreclosures spread out throughout the city; right? The 100 foreclosures that are spread out throughout the city might in fact have a greater overall dollar cost because they are near more properties. They are driving down the values of more properties.

So you really have to look at both the question of concentration and the total number affected by the foreclosures.

Mr. KUCINICH. Just a final followup question, here. The research that you've been involved in shows that the depression of housing values increases as the number of foreclosed property in close proximity increases. Would it be typical that in a given county or metropolitan statistical area or State, you'd find certain neighborhoods that have higher concentrations of foreclosures than others, or is it typical that you would find foreclosures equally distributed over large areas?

Ms. BEEN. No, foreclosures are very, very concentrated.

For example, in New York City, we have what we call 55 neighborhoods. In the last year, half of the foreclosures were in just nine of those neighborhoods. They are very highly concentrated. And the neighborhoods in which they are concentrated are the ones that have high rates of subprime lending; high rates of people of color, both blacks and Hispanics; high rates of other kinds of risky lending. So they are not evenly spread, they are very concentrated according to race and geography.

Mr. KUCINICH. Thank you very much.

I'm going to go to Congresswoman Watson.

Ms. WATSON. Just real quickly. Thank you, Mr. Chairman. I think you probably alluded to my questions.

What factors affect the likelihood that a property going into foreclosure will end up vacant? And what factors affect the duration

that a property remains vacant? And let me send this one over to Professor Been.

Ms. BEEN. The main factor that affects whether a property goes—becomes vacant is the strength of the housing market. Right?

Where you've got hot markets, strong—strong demand, then the property will be purchased or rented out, you know, fairly quickly. So the strength of the property market is really the main determinant.

But other things that will come into play is, again, the concentration. It is likely that the concentration of other foreclosed properties will affect it because they add to the housing supply. Right? They make many more houses be available to the purchaser who is looking. So that may affect the propensity of a property to actually go into vacancy.

In terms of how long they stay in vacancy, again, it's going to be the strength of the property market, which is going to depend upon things like the supply of the housing, what is going on in the broader market. So it really depends very strongly on the state of the market.

And of course, those things are related. The more foreclosures, the more risk that the market is going to fall.

Ms. WATSON. Mr. Chairman, thank you so very much for this hearing.

We've got votes on the floor, so I'll yield back my time.

Mr. KUCINICH. I thank the gentlelady.

We're going to take a recess since there are votes.

At the conclusion of votes, we'll come back, and I'm sure that's true of the other Members who have been present.

Do we know how many votes there are?

Four?

I would say we're probably looking at at least a half hour, maybe 40 minutes. So why don't we generally try to be back here by 20 after 4, and then we'll proceed with another round of questioning from the witnesses in a second panel, and then we'll go to the next panel.

I just want you to think about this, though, on this break that's coming up. Again, I want—I would like to have a further discussion about this idea of the wealth accelerating upwards. There is a massive transfer of wealth going on. Somebody is making a lot of money here, has already made a lot of money. You know, we could be looking all the way up to hedge funds, and—but there are all kinds of other players. So I want to talk to you a little bit about that when I come back.

Thank you.

This committee is in recess subject to the call of the chair. See you right after the votes.

[Recess.]

Mr. KUCINICH. The committee will come to order.

I would like to go back to Professor Been.

You've stated that there are differences between the effects of foreclosures and vacant buildings in hot markets versus cool markets. What are the important differences between foreclosures in vacant properties occurring in one market or the other? And in what ways should Federal intervention differ in those so-called hot

versus cool markets? And do you think the amount of aid, say on a per capita basis, should be different for a hot market versus a cool market?

And if we could start by defining terms here. Hot market.

Ms. BEEN. OK, a hot market is one in which property prices are generally appreciating or at least staying stable. But generally it is considered the property prices are appreciating.

The difference between a hot market and a cold market in terms of foreclosures is that if the market is hot, if you can turn around and sell your property when you—when a borrower goes into distress, can't afford the loan, has some, you know, personal crisis that makes them unable to afford the loan, they can usually sell the property and walk away without going into foreclosure, risking their credit rating and that kind of thing.

If it's a cold market and there's no market for the property, then they don't have that option. And so they may very well then end up in foreclosure because they can't sell the property.

So the other difference between hot markets and cold markets is that once property does go into foreclosure, in a hot market, it's less likely to sit vacant for a long time, because the bank is going to be able to sell it. There's going to be a buyer at auction, or there's going to be what we call a short sale.

Mr. KUCINICH. Do you think there is any difference—should those markets be treated differently in terms of providing any kind of Federal aid or intervention?

Ms. BEEN. Well, I don't think so. I think you have to be very careful there for a couple of reasons.

One is that you have impact from foreclosures on neighboring properties even in hot markets, meaning the research I reported was in New York City. New York City has been, knock on wood, a very hot market up until now. But you still see impacts of foreclosures, and that's because even though a property isn't remaining vacant or going through the entire foreclosure process, the maintenance is still often lower, the stability of the neighborhood is lower.

Mr. KUCINICH. Right.

Ms. BEEN. So it still has an—sends a message. Right?

Mr. KUCINICH. Thank you.

Mr. Talmage, you've done a lot of work in Detroit, Cleveland, St. Louis, among other places. These are long-suffering locations where rising vacancies have been a problem.

Has the fact that these cities had preexisting vacancy problems at all, has it insulated them at all from the effects of the subprime mortgage meltdown?

Mr. TALMAGE. No, I don't think it's insulated it. In fact, I think——

Mr. KUCINICH. Exacerbated it?

Mr. TALMAGE. Exacerbated it. You know, in the case of Detroit, where you've declined from a population of 2 million to 1 million——

Mr. KUCINICH. Could you make sure that mic is on?

Mr. TALMAGE. Yes, sir. I this better?

Mr. KUCINICH. OK, that's good.

Mr. TALMAGE. In the case of Detroit where you—the population has fallen from 2 million to 1 million in 50 years, that you already

had a blighted property situation to begin with, whole tracts of the city are blighted; that by adding another 35,000 foreclosures onto those rolls in the last 2 years, that the velocity of decrease has changed much more rapidly than other places, such as cities along the East Coast.

Mr. KUCINICH. How would foreclosures that occurred let's say in say 2000 or, you know, a little later show up today in neighborhoods? Would they be vacant? Would they be owner occupied?

Mr. TALMAGE. Would they be vacant or owner-occupied? I think that the foreclosures——

Mr. KUCINICH. What was it like in 2000?

Mr. TALMAGE. In 2000, you had—you had new, I'll use Detroit as my example. The city of Detroit had led the MSA in the number of transactions for the last 5 years, meaning that the number of home sales that were being transacted was the highest rate then of any of their surrounding communities.

The number of new housing permits and rehabilitation permits led that MSA as well for the same period. The foreclosure rate, and you can see the velocity of the number of homes that were provided high-cost loans increased from 2003 to 194, and then 195, and then 196. And that velocity has increased more, you know, and at tremendous speed. So I think that when there really—we're going to see 60,000 foreclosures in the city of Detroit this year, that impact will have a much higher impact on values of other community assets, whether it's households or not, than anything we could have forecasted today. So you see a velocity trend occurring that we haven't seen the bottom yet.

Mr. KUCINICH. Professor Been, I think I remember in your discussion, and maybe Ms. Betts got into it as well, the greatest amount of subprime loans went into areas that have been—that are primarily minority, African-American, in many cities, like in my city of Cleveland. We have seen other counties similarly situated, perhaps in communities that you talk about in Shelby County.

Ms. BEEN. Yes.

Mr. KUCINICH. Let's go back a little bit, 30 years ago or a little bit longer, President Carter saw the Community Reinvestment Act come forward, affirmative obligation on the part of lending institutions to lend money into communities that had previously been denied credit or been red lighted. OK? Is it in your—in your—in your estimation or anyone here, was the—the lending institution certainly knew where they weren't spending money. Is it possible that someone just—you know that lending institutions looked at a map, in your estimation, and determined, well, you know, we haven't loaned money here, and we're not in compliance with the Community Reinvestment Act. We'll package these subprime loans, send them out there, and who cares if anybody can pay them off or not. Have any of you thought about that at all.

Anyone want to try?

Ms. BETTS. I've actually looked at that quite a bit. Our local retail banks, which are the ones that were to be scrutinized under the Community Reinvestment Act——

Mr. KUCINICH. Talk closer to the mic, ok, bring the mic closer.

Ms. BETTS [continuing]. Our local retail banks are responsible for less than 20 percent of the originations, mortgage originations in Shelby County. The slack has been taken up by the national independent mortgage companies, most of which are not depository institutions, which are regulated in a different way. The local retail banks have been able to stick with the most lucrative business locally and basically have not been held accountable for the kind of lending neighborhood to neighborhood that was originally envisioned by the Community Reinvestment Act. The breach was filled by this other set of lenders. And some of us, in fact, talk about predatory green lining. It was almost as though we drew a green line around these particular neighborhoods and targeted them for these particular kinds of loan products.

Mr. KUCINICH. I would like—does anyone else have a response to that?

Mr. TALMAGE. I would just echo that I think Phyllis is absolutely right, that, in Cleveland, it wasn't the actions of Key Bank, or in Detroit—I mean, by larger numbers than what she was saying in Memphis, that the amount—the number of loans, the percent of loans that were given by the unregulated broker community far exceeded what national averages were. So I think that if you were to look at, you know, a market in itself or a census block in itself of where those loans originated from, that you would come back and say it is clearly the unregulated community.

Mr. KUCINICH. I think it is really important for this subcommittee to, as we get deeper into this issue of subprime, to look at where the mortgages originated. They may vary community by community, but clearly, at some point somewhere in some market, somebody made a decision and said, if we can write tens of millions of dollars in subprime loans, forget the documentation. We can then sell those upstream, capitalize on them, and who cares what happens afterwards. I mean, at some point—somebody did that at some point, and we're going to keep tracking that in this committee.

What I would like to do, and I'd like the members of panel, if you find and area that you think is worth looking at in the communities that you've worked with or that you studied, we'd appreciate any kind of amendment to your testimony or addendum that we could include in what you've already contributed, which has been pretty significant.

Mr. Tierney, did you have a followup question?

Mr. TIERNEY. Just a couple of wrap-up questions.

Mr. KUCINICH. Yes, please.

Mr. TIERNEY. Ms. Been, if we wanted to identify the external effects of foreclosures, what would be the appropriate unit of analysis? Would a zip code level be better than a county? Would a census tract be better than a zip code, or would a block be better than a census tract? What's the right analysis of vehicle to use there for purposes of where we should direct the Federal funds?

Ms. BEEN. Generally, in thinking about the external effects, you want to think about the neighborhood. And the unit that maps on, imperfectly, but maps on best is typically a census tract. Now, you don't always have data by a census tract. And then you tend to go up to a zip code and then to county level, but you really want to

start at the neighborhood. I mean, neighborhoods across a city are very, very different. So if you look at a city as a whole or a county as a whole, you're going to miss a lot of variation in what it is that those neighborhoods need.

Mr. TIERNEY. In keeping with that, I think we just ought to put something on the record of what's simplistic to all of us. And if we want to bring these things down to the—the values right down to the label of neighborhood pocketbook on this, if a neighbor had equity in a house that was about 28 percent of value, and then his house lost that 28 percent of value because the property next to it was vacant, they would essentially be wiped out. They've lost all that savings. They've lost whatever wealth they had in their house; right?

Ms. BEEN. They've lost—if they try to sell the house, they certainly will not make as much as they would otherwise.

Mr. TIERNEY. Right. If that's all they had, they're obviously in pretty dire straites. So I think that the record can reflect that foreclosure crises, when you have a lot of vacant properties, they robbed a number of neighbors of their wealth on that?

Ms. BEEN. Yes.

Mr. TIERNEY. So the long-term consequences for a community like that, what societal consequences of these neighbors losing their equity in that way do you foresee?

Ms. BEEN. Well, I think the societal consequences are several fold. One is, when we see what that looks like, it looks like the Bronx in the 1970's, where you have neighborhoods that are pockmarked by abandoned buildings. And it is very hard to get that neighborhood back together.

The second major societal consequence is that these are neighborhoods that, during the 1980's and the 1990's and this decade, we poured massive amounts of city, State and Federal investments in, and that's going to be lost. That's taxpayers' money that, you know, is going to be lost. And it is not just government money, but it's private investment, it's foundation investment that's all being wiped out.

Mr. KUCINICH. Would the gentleman yield?

Mr. TIERNEY. Yes.

Mr. KUCINICH. You know, in connection with that, this is very significant part of our discussion, because I can go back to my own neighborhood, my own district in Cleveland, and for example, there is an area call the Four City Park area. There were several parks in the community, and you can see when there's a decline in the residential housing stock, the infrastructure, the public infrastructure, experiences a similar decline. So there is lots of value. You can actually see it. And that's something that when we talk about the transfer of wealth, that's a transfer of wealth from the public, away from the public.

So, Mr. Tierney, thank you. I yield.

Mr. TIERNEY. Ms. Betts, Mr. Talmage, do you want to add anything to that or have we pretty much covered that ground?

Ms. BETTS. I would just underscore that, in a lot of markets, and I would look at medium-size cities in the South and Midwest in particular, not so-called rust-belt cities, where middle-income neighborhoods that didn't get actually a lot of the Federal money

and that have been a substantial source of the tax base and the primary source of wealth-building for all of those families in the middle, that if we increasingly have upscale neighborhoods and downscale neighborhoods, then the impact on the individual families will be difficulty in wealth-building that can be passed from generation to generation. And the impact on neighborhoods will be that if you're not in an upscale neighborhood, then you're going to be experiencing a lot of the issues that the neighborhoods that Professor Been has talked about have experienced for years. And I don't think that's where we want to go with our cities.

Mr. TIERNEY. Mr. Talmage.

Mr. TALMAGE. I would—also I think that the unit of analysis should always be at the block group level if not the household level. I do think that the data exists. It is hard to come by. It is not necessarily formatted for this use, but I think that's something that can be addressed.

But on the social impact, I think one of the things that we see in the cities that we're working with around the country is that there is a tremendous amount of pressure on cities to begin decommissioning neighborhoods, to remove public services from entire communities. And you know, this is something that the Bronx thought about back in the 1970's. And I think that kind of public policy agenda, it could have a long-run consequence that would accelerate some of the household wealth impacts that we've seen—we've seen over the last decade by for—not forcing but asking neighborhood communities or individual households to relocate to other neighborhoods where they are not connected to or whatnot. And I think that is the law of unintended consequences that if we don't sort of grapple with it now, understand what the impact is at the household level and at the neighborhood level, that some of these very bad public policy decisions will move forward.

Mr. TIERNEY. Thank you.

Mr. Chairman, may I ask one more closing question over my time a little bit here.

Mr. KUCINICH. Of course.

Mr. TIERNEY. Mr. Talmage, in your written testimony, you thought that the value of the equity stripped in Detroit was about a billion dollars.

Mr. TALMAGE. Yes, sir.

Mr. TIERNEY. Do you have an estimate of what you think it is nationwide?

Mr. TALMAGE. No, but we have a methodology to get to that.

Mr. TIERNEY. I bet you do.

Thank you very much.

I yield back, Mr. Chairman.

Mr. KUCINICH. I thank my colleague.

Again continuing this discussion about infrastructure, I mentioned a park and how that's deteriorated. But also think about this in terms of neighborhoods because you have an investment of a public infrastructure, a water system, a sewer system, electricity, telecommunications; that's all there.

If people are—if no one's—if there's a substantial decrease in the population of an area because of foreclosures, there is a loss of revenue to those companies. And also the infrastructure can deterio-

rate as well and which requires greater repairs. You can see the damage when you go into some of these communities. So it can be a public loss of revenue, which actually can turn around and increase the cost to other ratepayers if it is a utility, because you know what, you have less ratepayers. And it can increase the cost of water and sewer as well. So you have a cycle here of cost transfers that just sometimes seems not to end.

I'm grateful for the panel's participation. We'll have some followup questions from the committee staff after this hearing, I can assure you. And the quantification that you bring to this discussion is extremely important, and it is going to be very useful as this committee continues to go further.

We are going to dismiss the second panel with the thanks of the subcommittee and call the next panel forward. Thank you very much.

As the third panel is taking its place, we're fortunate to have outstanding witnesses on our third panel.

We have Mr. Alan Mallach, is the senior fellow at the National Housing Institute. His work focuses on housing and community development policy issues, including vacant and abandoned property issues, housing investment strategies, market-based urban regeneration. In 2006, Mr. Mallach published a book on abandoned property strategies entitled, "Bringing Buildings Back: From Abandoned Properties Into Community Assets."

Mr. Doug Leeper is the code enforcement manager for the city of Chula Vista, CA. He's owner of the Code Enforcement Solutions consulting firm. Over the course of his career, Mr. Leeper has supervised the enforcement of 30,000 cases; 1,100 warranted abatements; and 275 warranted demolitions.

Mr. Dean Baker is the cofounder and codirector for the Center for Economic Policy Research. He has previously worked as a senior economist at the Economic Policy Institute and assistant professor as Bucknell University. Dr. Baker has authored numerous books and articles, including his recent publication entitled, "The United States Since 1980." Dr. Baker earned his Ph.D. in economics from University of Michigan.

I want to thank the witnesses for appearing in front of the subcommittee today. It's the policy of the Committee on Oversight and Government Reform to swear in all witnesses before they testify. Please rise and raise your right hands.

[Witnesses sworn.]

Mr. KUCINICH. Thank you very much, gentlemen.

Let the record reflect that the witnesses have answered in the affirmative.

And I would ask, as in previous panels, that each witness give an oral testimony, a summary of your testimony, keep the summary under 5 minutes in duration.

Please keep in mind that your complete written statement will be included in the hearing record, so we won't miss a word of what you have to tell us.

Mr. Mallach, if you'd like to start.

STATEMENTS OF ALAN MALLACH, SENIOR FELLOW, NATIONAL HOUSING INSTITUTE; DOUG LEEPER, CODE OF ENFORCEMENT MANAGER, CITY OF CHULA VISTA, CA; AND DEAN BAKER, CO-DIRECTOR, CENTER FOR ECONOMIC POLICY RESEARCH

STATEMENT OF ALAN MALLACH

Mr. MALLACH. Thank you Mr. Chairman and members of the committee.

Mr. KUCINICH. And please pull that microphone closer, so we can hear you.

And if staff would assist Mr. Mallach in making sure that the microphone is on.

Please proceed.

Mr. MALLACH. First, I want to commend the committee for tackling this issue and also for focusing on the neighborhood and property aspects of these issues, which are so often overlooked.

I would like to suggest that tackling this issue really requires two separate types of action. One is to enable capable local governments and nonprofits to get control of properties, so they can be properly maintained and properly reused. But the other part is actions to minimize the harm that vacant properties do while they are vacant and before they can be re-used.

I would like to touch on both of these very quickly. Every city, town, county in this country has the ability to minimize harm from vacant properties through its code enforcement and nuisance abatement resources. And every State gives communities power in these areas, but many communities don't do this for a number of reasons. One, they lack the resources for effective code enforcement. Second, their programs are poorly organized or ineffective. Third, for financial or other reasons, they are unwilling to use their powers, particularly to step in where the owners won't maintain their properties.

And the foreclosure issue has added a fourth problem, which I think a previous speaker alluded to, which is this extended period of limbo where nobody is responsible. And while I know Chula Vista has attacked this issue, in most parts of the country, it is not being addressed because there is no law, no body of law that clearly makes lenders who have initiated foreclosures take on the responsibility for properties if the borrower has vacated the property. And without this, in many States which have judiciary foreclosure processes, the process can take anything from 9 months to over 2 years, from the point where the foreclosure starts to the point where title actually passes. And during this period, these properties typically fall in limbo. They are abandoned. They deteriorate. And by the time that title passes—if it ever does pass, which in many cases is not the case, because in some communities, and I know this happens in Cleveland, lenders will initiate the foreclosure, but may not aggressively pursue it, and the property will sit in limbo essentially forever.

So cities need help in developing the ability to enforce their codes to undertake nuisance abatements, to go after the people who are responsible and hold them accountable. And this is something where the Federal Government is not going to be able to do it, but

a very small amount of money directed at building local capacity and helping them in this area could reap enormous dividends in terms of helping to mitigate harm.

The second area is the question of controlling the properties. And here I would differ from a previous speaker with respect to the weak market versus strong market or hot versus cold issues. In hot markets, first, if a property goes into foreclosure in Palo Alto or Scarsdale, New York, the lender is going to make sure that it maintains its value, and once title passes, the odds are that it will go very quickly into the hands of a responsible buyer. There really is less need for money to acquire properties on the part of the public sector or the nonprofit sector where there is a strong market environment.

In Cleveland, in Detroit, in Buffalo, the lenders are not doing that. The properties are going into limbo and money is needed, resources are needed to acquire those properties if they are not going to continue to harm the community. So I think there is a significant difference in that respect between hot markets and cold markets.

But I think the other issue is that money is not the only issue. Yes, local governments, nonprofits need money to acquire properties, but at this point, in many cities, the capacity, both to acquire, maintain, manage and dispose of properties responsibly, simply does not exist. If you gave money in many cities, they would not be able to spend it responsibly.

A second or a third issue, rather, which is equally important is getting the people who control these properties to the table. To my knowledge, at this point, while there have been a few transactions around the country where lenders or servicers have sold small bundles of properties after they've taken title to nonprofits or local governments like the Michigan State Land Bank. I don't think there's been a single case where a local government or a nonprofit has successfully negotiated the sale of paper, the mortgages prior to foreclosure with a lender. And yet if you wait to the point where it is an REO, a real estate owned property, and then, only then start negotiating, the odds are that the property will have significantly deteriorated.

A recent national survey of realtors found that over 50 percent of the REO properties that got into the hands of realtors had already suffered significant property damage. And this is a cross section, of not just the Clevelands and Detroits, but of the Las Vegases and the Palo Altos and the San Diegos.

So unless we can figure out a way—or to put it differently, Congress can figure out a way—to motivate lenders, servicers, the people in the financial industry to negotiate seriously and responsibly with people who will take the paper and take responsibility for these properties, we will see this problem continue to mushroom.

And again, and this goes also to the question of how resources are allocated. This is—this is not an issue that is even for all foreclosures. All foreclosures are bad, but foreclosures in Las Vegas ultimately will be resolved by the economic growth and the job growth in the Las Vegas area. Foreclosures in Dayton or Buffalo will not be.

So, again, thank you for your attention, and I hope that this is useful.

[The prepared statement of Mr. Mallach follows:]

TESTIMONY
OF
ALAN MALLACH
"NEIGHBORHOODS the BLAMELESS VICTIMS of the SUBPRIME MORTGAGE CRISIS"

DOMESTIC POLICY SUBCOMMITTEE
OVERSIGHT AND GOVERNMENT REFORM COMMITTEE
WEDNESDAY, MAY 21, 2008
2154 RAYBURN HOB
2:00 P.M.

Chairman Kucinich, Ranking Member Issa, and Members of the Subcommittee.

My name is Alan Mallach. I am a Visiting Scholar at the Federal Reserve Bank of Philadelphia, and will be joining the Metropolitan Policy Program of The Brookings Institution as a Visiting Nonresident Fellow as of July 1 of this year. I have been working on the issues affecting urban neighborhoods in general, and on vacant and abandoned properties in particular, for much of my adult life, as a public official, advocate and scholar. I am the author of *Bringing Buildings Back: From Abandoned Properties to Community Assets*, published in 2006, which is the most comprehensive, systematic examination of this issue available.

I am pleased to have the opportunity to testify before you with respect to how best to address the neighborhood effects of vacant and abandoned properties, particularly in light of the dramatic increase in the number of such properties that is taking place as a result of mortgage defaults and foreclosures.

The devastating impact of vacant properties on neighborhoods, particularly urban neighborhoods with weak housing market conditions, has been well-documented. Vacant properties undermine property values, discourage investment, increase the risk of crime and fires, and create health hazards. The foreclosure crisis that is sweeping the United States has rendered thousands of properties in America's cities vacant, devastating many once-stable neighborhoods, or areas such as Cleveland's Slavic Village or Mt. Pleasant neighborhoods, which over recent years have fought back against decay, and gained a measure of vitality. Hundreds of other neighborhoods are at risk.

Successfully tackling this issue will require action in two separate arenas. Strategies are needed to enable capable local governments and non-profit entities to gain control of abandoned properties, so that they can be reused in ways that benefit the community and its residents. At the same time, actions must be taken to minimize the harm that these properties do to their surroundings during the period – which can be a long one – before they are reused, while they remain vacant,. I would like to address both of these areas.

Minimizing harm from vacant properties

A community's ability to minimize the harm from privately-owned vacant properties is a function of its ability to enforce its codes and abate nuisance conditions. If a city can effectively make property owners clean, secure, and maintain their properties – and step in to do the work if the owner fails to do so – they can dramatically reduce the harm those properties do, while taking the long-term steps needed to put them back to use. This is typically the responsibility of each city or county, which is given the auhority to enforce codes and abate nuisances by state law.

There are a number of reasons, however, why this system is not working well in many cities in the current crisis:

- ***Many cities lack the resources to provide effective code enforcement.*** With too few inspectors, prosecutors and support staff, they have been overwhelmed by the volume of vacant properties created by the foreclosure crisis.
- ***Many cities' code enforcement programs are poorly organized and ineffective.*** Inspectors may be poorly trained or supervised; technology, which could dramatically increase productivity, is not used, or used poorly; courts have backlogs, or give code matters low priority.
- ***Cities are unwilling to use their powers to abate nuisance conditions***, either because of lack of capacity or the difficulty of recovering their costs.

A fourth problem has arisen more recently as a result of the foreclosure crisis. In many states, foreclosure is a slow process, taking anything from nine months to over two years. Many homeowners facing foreclosure do not wait for what they consider to be inevitable, and abandon the property long before the sheriff's sale. The owner disappears, but the foreclosing lender or servicer is unwilling to take responsibility for the property. The property falls into limbo – a state that can last for years.

A small but growing number of states and cities, including Buffalo, Boston and some California cities, are holding the foreclosing lenders responsible for these properties, but most state laws do not permit this. *We need clear law that establishes that once a lender has asserted its control over a property by initiating foreclosure, it also takes the responsibility that goes along with that control, if the owner is no longer in the picture.* Cities should be able to hold lenders responsible for repairs, and if the lender fails to do so, correct the violations itself and go after the lender for the cost.

Cities need help, though, in building their capacity to enforce the codes and abate nuisances. A small amount of federal money could make a huge difference. One or two million dollars won't acquire or demolish that many properties. Used to hire inspectors or prosecutors, or enable cities to set up systems to use their existing resources efficiently, it could help preserve hundreds of properties.

Taking control of vacant properties

It is now widely recognized that preserving urban neighborhoods requires that qualified, capable local entities gain control of the thousands of vacant properties that have been created through subprime mortgage defaults and foreclosures. Without such steps, these properties will languish, particularly in weak market cities. While banks and mortgage companies may spend money to preserve the value of their REO assets in San Diego or Las Vegas, they are not doing so in Cleveland or Detroit. Effective measures to gain control of vacant properties, and properties at risk of abandonment will require that policymakers address three separate issues:

- Money for property acquisition
- Local capacity to acquire, manage and dispose of massive property inventories; and
- A willingness on the part of lenders and servicers to negotiate reasonable terms to transfer property to local entities.

Congress has taken important first steps with respect to providing money to local entities, with one caveat to which I will return. The other two issues, however, remain serious potential stumbling blocks.

Few cities or counties, and even fewer community development corporations and other nonprofits, have the capacity to handle thousands, or even hundreds of vacant properties. While a few, like the Land Bank in Genesee County, Michigan, can do so, other cities and counties don't even know what properties they already own, or what condition they're in. In addition to money for acquisition, assistance is needed to build the capacity – in both local government and the non-profit sector – to acquire, manage, maintain, and ultimately dispose of these properties.

Second, local governments and non-profits are still having a hard time getting lenders and servicers to come to the table, and negotiate transactions that reflect the true value of the properties or the cost of foreclosure. Whether this is from fear of legal repercussions, or more plausibly, because the industry is still in denial about the ultimate financial fallout from the unfolding crisis, is unclear. Either way, without them at the table, reuse strategies may be stillborn.

While local players can make headway here and there, a timely solution to this problem is likely to need federal action. Some combination of carrots and sticks may be needed. Much as it goes against the grain to provide *any* incentives to an industry that bears the brunt of the responsibility for a crisis that is destroying millions of lives and hundreds of communities, the fate of many of these communities hinges on how this issue can be resolved.

Finally, I would like to turn back to the question of the money that is likely to be provided for property acquisition. All foreclosures are unfortunate, but all foreclosures are not equal. What happens to vacant properties – and how much they end up costing the community – depends heavily on the regional economy. In Las Vegas, as a recent article in *Governing* magazine pointed out, local officials are counting on job growth to fill up most if not all of the vacant houses in the next year or two. Officials cannot make that

assumption in Dayton, Flint or Buffalo. Properties there will have to be held longer, maintained longer, and ultimately either demolished or rehabilitated before they can be put back to productive use. I strongly suggest that any formula that is used to allocate federal money for property acquisition and related costs reflect the difference in economic and housing market conditions between the different regions of the United States.

Thank you for your attention. I look forward to your questions.

Mr. KUCINICH. Thank you very much, Mr. Mallach.

Mr. Leeper, please proceed.

STATEMENT OF DOUG LEEPER

Mr. LEEPER. Thank you, Mr. Chairman. It's an honor to be here, and it's an honor to represent the code enforcement profession throughout the United States.

In anticipation of the record number of potential foreclosures on the horizon, the city of Chula Vista drafted and passed an abandoned residential properties ordinance. Vacant property registration ordinances are nothing new and have been existing in some cities for decades. The Chula Vista ordinance had a slightly different reason and focus: the black hole or the limbo we've spoke of before between default and foreclosure sale. When in many cases the home sits empty, the borrowers are gone, and the lender won't take responsibility for it, this is the period of time when a great deal of damage and deterioration can occur.

Although the lenders claim they have no rights to the property prior to the actual foreclosure sale, we found the opposite to be true. This truth came in the way of a standard clause within the mortgage contract, commonly referred to as the abandonment and waste clause. Simply put, the clause allows lenders to secure and maintain property against vandalism, theft and waste. The borrower stops making payments and moves out. In short, they abandon the property.

Lenders don't like to exercise this right, and in many cases won't admit that it exists. The Chula Vista ordinance, nicknamed the "good neighbor ordinance," simply requires the lenders to secure and maintain their investment, which in turn helps stabilize the surrounding neighborhood; in short, be a good neighbor. After all, what would they want done if it was across the street from their house or next door to their child's school? They would want it maintained to the neighborhood standard. That's what our ordinance requires: security and maintenance to the neighborhood standard.

As the committee is aware, a law without consequence is merely words on paper. The consequences for violation of the Chula Vista ordinance range from criminal prosecution, not feasible in most cases, fines or abatement.

Chula Vista did not budget for becoming the gardener and property manager for the 2,000-plus vacant abandoned properties we have now, and with the downturn in the economy, whatever we're calling it, we don't have the means to do it now. Our single best option: to gain the attention of the lenders with monetary fines and penalties.

As a code enforcement manager, my bottom line is people, quality of life, neighborhood livability. The lenders' bottom line is dollars. So until it became more expensive for them to ignore us than to properly maintain their properties, they continued to ignore us.

Early on we were informed by the lending industry that we couldn't pass such a law and that they wouldn't adhere to it. Registrations were slow at first, but with the first round of penalties ranging from $3,000 to $10,000 per property, lenders soon acknowledged that the city of Chula Vista meant business.

Currently there are approximately 450 properties registered in Chula Vista. Most are in compliance with the neighborhood standard and are posted. We require posting of a name and phone number of a local contractor responsible for the upkeep of the property so neighbors don't have to rely on the city to call, they can call directly to the responsible party if there's a problem with the property.

Unfortunately the rate of foreclosures and vacant properties has accelerated past six a day, but our staffing remains the same. I was forced to realign resources and suspend enforcement on other important issues to address the disgrace of abandoned properties. And if it continues at this rate, I'll have to do it again, leaving other issues unaddressed.

One of the reasons these are difficult to deal with is the research required to track down the current beneficiary of the mortgage. These notes rarely stay with the party of issuance. They are bought, sold and traded like baseball cards. Rarely, if ever, does the new beneficiary, be it a lender, a mortgage company, a trust or a security, record their newfound interest in the property. This leaves the local jurisdictions grasping at straws in an attempt to locate someone, anyone that will admit to holding an interest in the property.

One of our first problem properties came by way of a $30,000 fine for noncompliance while the initiator, the originator of the loan, argued with the entity they sold it with as to who was responsible. The property sat vacant and vandalized for 3 months before they finally decided. They then spent $16,000 to bring the property in compliance and asked that I waive their fines and penalties. I did not.

Due in part to its new focus, Chula Vista's ordinance received some press and attention from other cities, almost 200 cities throughout the Nation. The California State Assembly is considering passing legislation based on Chula Vista's ordinance. The cost to local jurisdictions from this foreclosure fallout is near incalculable: HOA dues, homeowners' dues, go unpaid and services go undone; delinquent taxes; reduced property taxes; increased calls for service through theft, vandalism, fraud and arson; increased insurance rates for neighbors; reduction in other city services; and displaced renters.

I was recently contacted by a young lady by the name of Esther who was in a panic. There was a default notice on her door. She was very upset because her husband is currently deployed with the U.S. Navy, and she didn't know what to do. We were able to get her in touch with the lender who holds the note, but all the while the landlord has been cashing their checks.

The U.S. Conference of Mayors, Department of Housing and Urban Development and the Mortgage Bankers Association all agree that one of these vacant, abandoned, unmaintained homes can have a negative financial impact for other homes within an eighth of a mile. What will the impact of 2 be, of 10, of 30?

These impacts are not only financial, but are also emotional as the American dream turns into a neighborhood nightmare, as brand new neighborhoods slip into blighted ghost towns, as other existing neighborhoods that saw redevelopment as a light at the

end of the tunnel find that light is now the train of foreclosures and abandoned properties.

I can't tell you the cost of my city, not yet anyway. I do know the problem is beyond my sleepy little San Diego suburb. It's national; red States and blue. I've heard estimates that we as a Nation may see as many as 2 million to 3 million foreclosures. That's equal to every single family home in the State of Missouri. Or at a rate of 3.75 people per home, that's the entire population of Georgia.

By all means, the best answer is to keep as many borrowers—better stated homeowners—who occupy the homes in their homes as possible. Short of that it will be left to the local jurisdictions to fight the war against vacant, abandoned properties; and as any battle requires weapons, like Chula Vista and troops on the ground, which none of us, at least none of the cities I've talked to, are prepared for. Thank you.

Mr. KUCINICH. I thank the gentleman for his testimony.

[The prepared statement of Mr. Leeper follows:]

Neighborhoods: The Blameless Victims of the Sub-prime Mortgage Crisis.

Written Testimony Submitted by:
Doug Leeper, Code Enforcement Manager
Chula Vista, CA

Earthquakes, cyclones, tsunamis and hurricanes, we hear of their destructive nature and see their devastating impacts on our evening news. Somewhere in the world people are impacted by these natural disasters daily. We, here in the US, are suffering under an un-natural disaster that is impacting hundreds of thousands of neighborhoods and millions of people – vacant, abandoned, accessible properties.

Although the collapse of the housing market and lending industry has been widely reported, the ripple out effect of the collapse has yet to be adequately addressed. There have been discussions on who is to blame and how to prevent this from happening again, but little attention has been paid to the true, innocent victims – the neighbors and local jurisdictions that are left to cope with and clean up the mess.

If a ship's captain recklessly pilots his ship into a hazard and spills oil, the damage isn't contained to just the ship. The oil spilled from that ship leaks into and spreads over miles of ocean, beaches and coastline. It seeps into every nook and crevasse. It covers every rock, every grain of sand. It coats unsuspecting wildlife and damages the environment for decades to come. Such is the case with the record number of financially distressed properties (foreclosures) we are experiencing across the Nation.

The SS Mortgage has run aground at the hands of reckless captains. The crude oil of foreclosures and abandoned properties has leaked into and spread over the entire country, neighborhood by neighborhood. Unsuspecting residents are being covered in the oil of diminishing home values, blight and unmarketable real estate. They find themselves mired in a situation they didn't create and yet can't free themselves from.

With shipwrecks and oils spills, the damage can be minimized by fast action and containment. There are federal, state and local laws that require response crews be trained to react. There are action plans and drills to prepare for the worst. Even with this training and response, the impacts are only "minimized". The damage can't be undone. And when all is said and done, it can take decades to calculate the cost of response, containment and recovery. But, with a single spill, at least there is someone to hold accountable.

This is not the case in the situation we find ourselves now, this "mortgage meltdown". While ships holds were filled to overflowing with mortgages, some very questionable, loading crews (brokers and originators) were hired in record number, and little, if any, thought was given to training response crews, preparing action plans or conducting drills. In short they didn't prepare for this disaster, they didn't feel they needed to. If a gallon or two of oil sloshed over the gunwales there would be someone there to scoop it up. In real estate terms, you could always "flip it", sell the house or mortgage, and save yourself from the "spill". You could, that is, until too much of the oil spilled over at once and there was no one there to scoop it up anymore.

This all could have been avoided, and even still the damage can be minimized, the spilled oil can be contained. But the beneficiaries of these mortgages (lenders, securities and trusts) claim they aren't responsible but are the victims, after all it's their ships that have been damaged. They aren't looking at the oil they have spilled onto unsuspecting bystanders living next door to or across the street from THEIR financially distressed abandoned properties.

A select few groups saw the impending collapse and attempted to prepare for the negative impact it would have. The City of Chula Vista was among those few groups. Realizing the City had seen unprecedented growth and housing sales, as well as a record increase in median valuation, City officials recognized their vulnerability to numerous foreclosed abandoned properties in the near future. Staff had experienced the non-reactive nature of the mortgage industry during the housing downturn of the early 1990's and drafted a pro-active abandoned property registration and maintenance ordinance that sought to minimize the negative impact these conditions bring.

See Attachment "A"
Chula Vista Abandoned Residential Property Registration Ordinance

The ordinance was unique, in that it wasn't based on the physical condition of the property alone but the contractual condition of the mortgage as well. Let me explain. In most states the lenders are required to file or record default/pre-foreclosure documents with the county in which the subject property is situated. The lender then must wait for a court date or, in non-judicial circumstances, a pre-determined number of days, before proceeding with the notice of foreclosure sale. In California it is 90 days. In many instances, the properties subject to the filings and recordations are vacant and abandoned during this "warning period."

After their court date, or the expiration of the mandatory time frames, the lender must file or record additional notices and advertise the pending foreclosure sale. In California this recordation and advertising must take place a minimum of 21 days prior to the actual sale. As stated before, many of the homes are vacant and abandoned during this period.

See Attachment "B"
Financially Distressed Property Foreclosure Timeline

It is during this time period, a minimum of four months in California, that a large majority of these vacant properties become the rotting tooth of the neighborhood smile as they are left to the elements and whims of passersby, vandals, thieves and the like. It is also during this time period that lenders claim they can't take ANY action on the property because they don't own it yet . . . it hasn't gone through foreclosure sale. They overlook the covenants within their mortgage contract that provide them that very right. This covenant is commonly referred to as an "Abandonment and Waste Clause" and in short it states that if the borrower stops making the mortgage payments and moves out of the house, leaves it vacant, the lender may access the property to secure it from vandalism,

deterioration and waste. The borrower agreed to this condition upon signing the mortgage contract. There are some restrictions on the lenders in these actions. They may not remove, alter or destroy the structure. They may take action as may be reasonably necessary to prevent unauthorized entry (re-keying locks, replacement of doors/windows, boarding, etc.). They may maintain landscaping, pools and fences. They must inventory and store any personal items they remove from the property. They cannot market or rent the property. And they may not deny the borrower access if they return and request it.

So, if lenders have the right to protect their investment, the house, why don't they? After all, they claim that they desire the same things the cities do, safe and stable neighborhoods. The short answer is money. In more detail there are about seven main reasons:

1. They hope the borrower remedies the default and makes up all the back payments and fees.
2. They hope property will sell prior to the foreclosure sale.
3. They hope to sell the mortgage to another lender.
4. They hope they are outbid at the foreclosure sale.
5. They hope the local jurisdiction will maintain the property for them.
6. They don't want to risk potential litigation from the borrower.
7. They have insurance that covers damage caused to the property prior to the foreclosure sale. This damage is sometimes referred to as "Mortgagor Abuse."

Chula Vista's new ordinance compels the lender or beneficial interest/mortgage holder exercise the abandonment clause in their contract. It simply states that upon recording a Notice of Default (pre-foreclosure action) the lender <u>must</u> inspect the property for occupancy. If the property is found to be vacant, the lender must register the property with the City and then begin to maintain the property to the neighborhood standard.

Why must the lender register the property with the City? There is an additional problem in the lending industry beyond the collapsing housing market and avalanche of foreclosures we are experiencing. The problem is difficult to explain but has a simple remedy.

The problem is an inability of local authorities to locate the current beneficiary of the mortgage/deed of trust. Mortgage brokers and lenders buy, sell and trade mortgage loans like baseball cards and Halloween candy. They always notify the borrower where to send their payments but rarely record the substitution of beneficiary or assignment of rents with the county to provide notice to anyone, such as a code enforcement department, that may need to communicate with the lender. When local officials review the title documents, in an attempt to locate a responsible party, quite often they are met with this outdated information that results in disconnected phone lines and dead ends.

<u>See Attachment "C"</u>
<u>Beneficial Interest Transfer Detail</u>

Although recordation of these one or two page documents would save government agencies countless hours and thousands of dollars in forensic research, at a minimal cost to the lender, most counties charge $10-$20 to record such documents, many lenders claim it is "cost prohibitive." Most states allow for the recordation of these documents but do not require them.

There is an alternative to recording these documents with the county. The Mortgage Electronic Registration System (MERS) is an Internet database that is accessible to all lenders. It works very much like the DMV. Each new mortgage is issued a Mortgage Identification Number or MIN. Much like a Vehicle Identification Number (VIN), no two are alike and they stay with the vehicle, in this case the mortgage, for its duration. The MIN is listed on the original mortgage (which ALWAYS gets recorded) making it accessible to local authorities as a public record. If the mortgage is sold, transferred or otherwise taken over, the previous beneficiary can release their interest electronically on the database and list the new beneficiary or in the reverse the new beneficiary can register their interest electronically minimizing the need for local recording. This type of registration removes the lender's argument that recording such information (documents) is slow and "cost prohibitive" as the electronic registration is live and can be preformed from anywhere in the world.

Armed with an original mortgage document, the local authority can access the MERS web-site, free of charge, and input the 17 digit MIN number. The database then provides the current beneficiary, their address and contact information. With current information code enforcement officers can communicate with the current beneficiary through issuance of a Notice of Violation and by phone in many cases. The faster the beneficiary is contacted, the faster the problem can be resolved and the faster we stabilize the neighborhood.

For far too long the lenders have abdicated their property management/maintenance responsibility and, by their inaction, transferred <u>their</u> job to the local authorities. Lenders were content to let code enforcement secure their properties, remove their trash, paint out their graffiti and even mow their lawns. Although most local jurisdictions have the authority and can perform these tasks summarily or under warrant, most cities, small and large, do not have the staff nor budget for such activities. Most jurisdictions send a bill for these services to the last known responsible party, but as stated above, rarely are these documents current. Some jurisdictions have the ability to lien the property for outstanding debts but in many states these liens are eliminated at the foreclosure sale. With that in mind the new ordinance also requires that lenders retain the services of a local property manager/maintenance company and that the company's name and contact phone number be visibly posted on the property. The posting serves several purposes. It removes the city from its position as de facto property manager and allows anyone that observes a problem at the property direct contact with an entity that can respond and address the issue.

The problems we have been experiencing are wide and diverse. In the worst cases children are abducted, raped and murdered. Bad things happen in vacant properties!

Some are targets for arson and insurance fraud. Theft and vandalism are the most obvious. Homes have been stripped of appliances, cabinets and carpet. With record prices being paid for scrap copper and aluminum, wiring and plumbing are almost irresistible to these thieves. Entrepreneurial college and high school students have, through the Internet, found a way to turn these vacant abandoned homes into makeshift one-shot nightclubs. Con-artists are advertising these homes for rent to unsuspecting families who pay thousands of dollars in cash only to find out they have no right to be in the home. Teenagers and gangs have taken over homes and trashed them, nearly beyond repair. But, all this is the "banks" loss, right? While on the surface it may seem so, the real cost is passed on the local community through increased calls for police and emergency services and reduced property values and marketability. Although the lenders maintain insurance on these properties, and receive settlement checks on a regular basis, these vandalized properties are rarely repaired to a marketable "move in condition" but are sold "as is" at a highly reduced rate. This practice lowers the comparable values of the remaining properties in the neighborhood. The reduction in neighborhood livability, value and marketability only serve to set the stage for more foreclosures, a self-fulfilling prophecy.

The US Conference of Mayors, HUD, VA and several other organizations have reported that ONE of these vacant abandoned properties has a negative financial impact on the surrounding community up to 1/8 of a mile away. The negative impact is multiplied when the number of these properties increases. In some neighborhoods we have already seen as many as one in five properties fall into this status. As these properties deteriorate the visual impact can lead to discouragement of neighboring property owners, who can begin to neglect their own properties. Blight breeds blight.

Armed with this information and a new ordinance, the City of Chula Vista hoped to minimize the negative impact in its neighborhoods, to stop the bleeding. At first officials were told, by the lending/foreclosure industry, that they couldn't pass or enforce such a law. The city moved forward. Soon after they were informed that the lending industry would fight the law. They did not. Next, they were informed that no one in the lending industry would follow the ordinance. The City began to issue notices and monetary penalties. The lenders started to take note. The new ordinance has gained notoriety and cities from all over the Nation have contacted the City asking for background information and examples. To date the City has received nearly 200 inquiries from other jurisdictions. As some of these cities began to pass similar ordinances, and Chula Vista continued to issue financial penalties, the lending industry, although reluctantly, began to respond. One sign that the City had gained their attention came in the way of a phone call to the Code Enforcement Manager at his home on a weekend. A high level representative of the lending/foreclosure industry informed him that he was, "making too much fucking noise" with the ordinance. Soon after, some lenders began to make contact with the City, in some cases sending representatives to California to discuss the ordinance and how they could best meet the compliance standards.

See Attachment "D"
List of Interested Cities

The City of Chula Vista has the highest foreclosure rate in San Diego County with an estimated 1,000 to 1,500 REO's (foreclosures) and an additional 2,000+ recorded defaults (pre-foreclosures). It is estimated that all the REO's and approximately 1/3 of the recorded defaults are vacant. That is a total of over 2,100 vacant abandoned properties. Although the ordinance authorizes staff to be pro-active and inspect every recorded default and REO, staffing levels don't allow for such activity. Officers are reactive and respond to resident complaints of vacant abandoned properties. Currently there are 450 properties registered in the program. About 10% (45) of those are in violation of the maintenance and/or posting sections of the ordinance. On the other hand we have noted several properties that are in compliance with the ordinance, clean, green, secure and posted, but not registered. These properties ARE NOT a priority with the staff. The City is less concerned with collecting the registration fee than the elimination of visual blight and attractive nuisances. Staff currently has approximately 100 open reactive cases in process.

Additional staff and funding sources were not available at the implementation of the program. Initially, 20% of existing reactive staff was assigned to the program. Recently we have increased that percentage as the number of foreclosures has accelerated. To date the program has generated $31,500 in revenue through registration fees ($70 per property). An additional $154,979 has been assessed in fines, penalties and full cost recovery. Of that, $25,519 has been collected the remaining $129,460 has been recorded as special assessment liens with the County Tax Assessor's Office. The total revenue received to date, $57,019, has nearly covered the cost of the program.

There were three challenges faced as the program was implemented:

1. **Notifying a multi national lending/foreclosure industry of a local ordinance/program.** – Response – The Code Enforcement Manager had previously been involved with the lending/foreclosure/loan and field servicing industry and had contacts within many of the national organizations such as the Mortgage Bankers Association, Real Estate Owned Management Association of California and the United States Foreclosure Network. With this information, getting the word out was not difficult.
2. **Locating the current beneficiary of the mortgage on a property that was in violation.** – Response – This remains one of the single largest obstacles in dealing with financially distressed properties. Often mortgage loans are issued and then the beneficial interest is sold to another company/lender, security or trust and that transfer is not recorded. Without a recorded transfer or substitution of beneficiary the local jurisdiction has no way to contact the individual or corporation that has authority over the property. The time spent in research and phone calls attempting to track down the current beneficiary is crippling.
   Note: The California State Assembly is currently reviewing a bill that would make recordation of such changes mandatory.
3. **Adequate staffing.** – Response – 40% of the reactive code enforcement staff (two officers) have been assigned to respond to vacant abandoned financially distressed properties only. We have enlisted the assistance of our building inspectors. They

monitor the registered properties for continued compliance and notify the code enforcement officers of violations. Other less urgent issues have been placed on a "Service Reduction List" of items we are currently unable to respond to. Admittedly this has the potential to create a backfire effect if the foreclosure crisis is prolonged.

Although there remains a vacant abandoned property issue within the City of Chula Vista, and vacant abandoned unmaintained properties can be seen in many neighborhoods, the negative impacts are being greatly reduced, as lenders understand there are serious financial consequences to non-compliance. Through this process we have learned that enforcement CAN reduce the negative impact these properties create. It is only when the cost of inaction, fines and penalties, are greater than the cost of proper maintenance and security that the lenders will "do the right thing" and pro-actively maintain the properties that THEY ARE RESPONSIBLE FOR.

Attachment "A"
15.60 ABANDONED RESIDENTIAL PROPERTY REGISTRATION

15.60.010 PURPOSE/SCOPE
It is the purpose and intent of the Chula Vista City Council, through the adoption of this Chapter, to establish an abandoned residential property registration program as a mechanism to protect residential neighborhoods from becoming blighted through the lack of adequate maintenance and security of abandoned properties.

15.60.020 DEFINITIONS
For the purposes of this chapter, certain words and phrases used in this chapter are defined as follows:

"Abandoned" means a property that is vacant and is under a current Notice of Default and/or Notice of Trustee's Sale, pending Tax Assessors Lien Sale and/or properties that have been the subject of a foreclosure sale where the title was retained by the beneficiary of a deed of trust involved in the foreclosure and any properties transferred under a deed in lieu of foreclosure/sale.

"Accessible property" means a property that is accessible through a compromised/breached gate, fence, wall etc..

"Accessible structure" means a structure/building that is unsecured and/or breached in such a way as to allow access to the interior space by unauthorized persons.

"Agreement" means any agreement or written instrument, which provides that title to residential property, shall be transferred or conveyed from one owner to another owner after the sale, trade, transfer or exchange.

"Assignment of Rents" means an instrument that transfers the beneficial interest under a deed of trust from one lender/entity to another.

"Beneficiary" means a lender under a note secured by a deed of trust.

"Buyer" means any person, co-partnership, association, corporation, or fiduciary who agrees to transfer anything of value in consideration for property described in an agreement of sale, as defined in this subsection.

"Dangerous building" means any building/structure that is violation of any condition referenced in CVMC Chapter 15.18.

"Days" means consecutive calendar days.

"Deed of Trust" means an instrument by which title to real estate is transferred to a third party trustee as security for a real estate loan. Used in California instead of a mortgage.

This definition applies to any and all subsequent deeds of trust i.e.: 2nd trust deed, 3rd trust deed, etc.

"Deed in lieu of foreclosure/sale" means a recorded document that transfers ownership of a property from the trustor to the holder of a deed of trust upon consent of the beneficiary of the deed of trust.

"Default" means the failure to fulfill a contractual obligation, monetary or conditional.

"Distressed" means a property that is under a current Notice of Default and/or Notice of Trustee's Sale and/or pending Tax Assessor's Lien Sale or has been foreclosed upon by the trustee or has been conveyed to the beneficiary/trustee via a Deed in lieu of Foreclosure/sale.

"Evidence of vacancy" means any condition that on its own, or combined with other conditions present would lead a reasonable person to believe that the property is vacant. Such conditions include but are not limited to, overgrown and/or dead vegetation, accumulation of newspapers, circulars, flyers and/or mail, past due utility notices and/or disconnected utilities, accumulation of trash, junk and/or debris, the absence of window coverings such as curtains, blinds and/or shutters, the absence of furnishings and/or personal items consistent with residential habitation, statements by neighbors, passersby, delivery agents, government employees that the property is vacant.

"Foreclosure" means the process by which a property, placed as security for a real estate loan, is sold at auction to satisfy the debt if the trustor (borrower) defaults.

"Local" means within forty (40) road/driving miles distance of the subject property.

"Neighborhood standard" means those conditions that are present on a simple majority of properties within a three hundred (300) foot radius of an individual property. A property that is the subject of a neighborhood standard comparison, or any other abandoned property within the three hundred (300) foot radius, shall not be counted toward the simple majority.

"Notice of Default" means a recorded notice that a default has occurred under a deed of trust and that the beneficiary intends to proceed with a trustee's sale.

"Out of area" means in excess of forty (40) road/driving miles distance of the subject property.

"Owner" means any person, co-partnership, association, corporation, or fiduciary having a legal or equitable title or any interest in any real property.

"Owner of record" means the person having recorded title to the property at any given point in time the record is provided by the San Diego County Recorders Office.

"Property" means any unimproved or improved real property, or portion thereof, situated in the city and includes the buildings or structures located on the property regardless of condition.

"Residential building" means any improved real property, or portion thereof, situated in the city, designed or permitted to be used for dwelling purposes, and shall include the buildings and structures located on such improved real property. This includes any real property being offered for sale, trade, transfer, or exchange as "residential" whether or not it is legally permitted and/or zoned for such use.

"Securing" means such measures as may be directed by the Director of Planning and Building or his or her designee that assist in rendering the property inaccessible to unauthorized persons, including but not limited to the repairing of fences and walls, chaining/pad locking of gates, the repair or boarding of door, window and/or other openings. Boarding shall be completed to a minimum of the current HUD securing standards at the time the boarding is completed or required.

"Trustee" means the person, firm or corporation holding a Deed of Trust on a property.

"Trustor" means a borrower under a deed of trust, who deeds property to a trustee as security for the payment of a debt.

"Vacant" means a building/structure that is not legally occupied.

15.60.030 RECORDATION OF TRANSFER OF LOAN/DEED OF TRUST/ASSIGNMENT OF RENTS

Within ten (10) days of the purchase and/or transfer of a loan/deed of trust secured by residential property the new beneficiary/trustee shall record, with the San Diego County Recorders Office, an Assignment of Rents, or similar document, that lists the name of the corporation, and/or individual, the mailing address and contact phone number of the new beneficiary/trustee responsible for receiving payments associated with the loan/deed of trust.

15.60.040 REGISTRATION

Any beneficiary/trustee, who holds a deed of trust on a property located within the City of Chula Vista, shall perform an inspection of the property that is the security for the deed of trust, upon default by the trustor, prior to recording a Notice of Default with the San Diego County Recorders Office. If the property is found to be vacant or shows evidence of vacancy, it is, by this chapter, deemed abandoned and the beneficiary/trustee shall, within ten (10) days of the inspection, register the property with the Director of Planning and Building or his or her designee on forms provided by the City.

If the property is occupied but remains in default it shall be inspected by the beneficiary/trustee, or his designee, monthly until 1) The trustor other or party remedies the default or 2) It is found to be vacant or shows evidence of vacancy at which time it is deemed abandoned, and the trustee shall, within ten (10) days of that inspection, register

the property with the Director of Planning and Building or his designee on forms provided by the City.

In either case the registration shall contain the name of the beneficiary/trustee (corporation or individual), the direct street/office mailing address of the beneficiary/ trustee (no P. O. Boxes), a direct contact name and phone number for the beneficiary/trustee and, in the case of a corporation or out of area beneficiary/trustee, the local property management company responsible for the security, maintenance and marketing of the property. Registration fees will not be prorated.

An annual registration fee shall accompany the registration form. The fee and registration shall be valid for the calendar year, or remaining portion of the calendar year, in which the registration was initially required. Subsequent registrations and fees are due January 1st of each year and must be received no later than January 31 of the year due.

This section shall also apply to properties that have been the subject of a foreclosure sale where the title was transferred to the beneficiary of a deed of trust involved in the foreclosure and any properties transferred under a deed in lieu of foreclosure/sale.

Properties subject to this chapter shall remain under the annual registration requirement, security and maintenance standards of this section as long as they remain vacant.

Any person, firm or corporation that has registered a property under this chapter must report any change of information contained in the registration within ten (10) days of the change.

15.60.050 MAINTENANCE REQUIREMENTS

Properties subject to this section shall be, in comparison to the neighborhood standard, kept free of weeds, dry brush, dead vegetation, trash, junk, debris, building materials, any accumulation of newspapers, circulars, flyers, notices, accept those required by federal, state or local law, discarded personal items including but not limited to, furniture, clothing, large and small appliances, printed material or any other items that give the appearance that the property is abandoned.

The property shall be maintained free of graffiti, tagging or similar markings by removal or painting over with an exterior grade paint that matches the color of the exterior of the structure.

Visible front and side yards shall be landscaped and maintained to the neighborhood standard at the time registration was required.

Landscape includes, but is not limited to, grass, ground covers, bushes, shrubs, hedges or similar plantings, decorative rock or bark or artificial turf/sod designed specifically for residential installation.

Landscape does not include weeds, gravel, broken concrete, asphalt, decomposed granite, plastic sheeting, mulch, indoor-outdoor carpet or any similar material.

Maintenance includes, but is not limited to regular watering, irrigation, cutting, pruning and mowing of required landscaped and removal of all trimmings.

Pools and spas shall be kept in working order so the water remains clear and free of pollutants and debris or drained and kept dry. In either case properties with pools and/or spas must comply with the minimum security fencing requirements of the Sate of California.

Adherence to this section does not relieve the beneficiary/trustee or property owner of any obligations set forth in any Covenants Conditions and Restrictions and/or Home Owners Association rules and regulations which may apply to the property.

15.60.060 SECURITY REQUIREMENTS

Properties subject to this section shall be maintained in a secure manner so as not to be accessible to unauthorized persons.

Secure manner includes but is not limited to the closure and locking of windows, doors (walk-through, sliding and garage) gates and any other opening of such size that it may allow a child to access the interior of the property and or structure(s). In the case of broken windows securing means the reglazing or boarding of the window.

If the property is owned by a corporation and/or out of area beneficiary/trustee/ owner, a local property management company shall be contracted to perform weekly inspections to verify that the requirements of this section, and any other applicable laws, are being met.

The property shall be posted with name and 24-hour contact phone number of the local property management company. The posting shall be no less than 18" X 24" and shall be of a font that is legible from a distance of forty-five (45) feet and shall contain along with the name and 24-hour contact number, the words "THIS PROPERTY MANAGED BY" and "TO REPORT PROBLEMS OR CONCERNS CALL". The posting shall be placed on the interior of a window facing the street to the front of the property so it is visible from the street, or secured to the exterior of the building/structure facing the street to the front of the property so it is visible from the street or if no such area exists, on a stake of sufficient size to support the posting in a location that is visual from the street to the front of the property but not readily accessible to vandals. Exterior posting must be constructed of and printed with weather resistant materials.

The local property management company shall inspect the property on a weekly basis to determine if the property is in compliance with the requirements of this chapter.

15.60.070 ADDITIONAL AUTHORITY
In addition to the enforcement remedies established in Chapters 1.20, 1.30 and 1.41, the Director of Planning and Building or his or her designee shall have the authority to require the beneficiary/trustee/owner and/or owner of record of any property affected by this section, to implement additional maintenance and/or security measures including but not limited to, securing any/all door, window or other openings, installing additional security lighting, increasing on-site inspection frequency, employment of an on-site security guard or other measures as may be reasonably required to arrest the decline of the property.

15.60.080 FEES
The fee for registering an Abandoned Residential Property shall be set by resolution of the City Council.

15.60.90 ENFORCEMENT
Violations of this chapter may by enforced in any combination as allowed in Chapters 1.20, 1.30 and 1.41.

15.60.100 APPEALS
Any person aggrieved by any of the requirements of this section my appeal insofar as such appeal is allowed under Chapter 1.40.

15.60.110 VIOLATION/PENALTY
Violations of this chapter shall be treated as a strict liability offense regardless of intent. Any person, firm and/or corporation that violates any portion of this section shall be subject to prosecution and/or administrative enforcement under Chapters 1.20 and 1.41.

15.60.120 SEVERABILITY
Should any provision, section, paragraph, sentence or word of this chapter be determined or declared invalid by any final court action in a court of competent jurisdiction or by reason of any preemptive legislation, the remaining provisions, sections, paragraphs, sentences or words of this chapter shall remain in full force and effect.

Attachment "B"
Financially Distressed Property Foreclosure Timeline
(California)

• Mortgage issued	
• 1st missed payment – "late"	30 days
• 2nd missed payment – "delinquent"	60 days
• 3rd missed payment – "seriously delinquent"	90 days
• Notice or Default – 1st step in foreclosure	120 days
• Sale Notice –	141 days minimum
• Sale –	

This is the timeline IF the lender is organized and has not lost track of their inventory. Most lenders are overwhelmed which leads to a much longer process.

Although the borrower, or tenant, may remain in the home throughout this process we have noted that approximately 1/3 of the properties in this process are vacant prior to the completion of the foreclosure.

Attachment "C"
Beneficial Interest Transfer Detail

- Mortgage broker issues a real estate loan to an individual.
- Mortgage broker records Deed of Trust w/county.
- Mortgage broker sells the loan to a larger mortgage company.*
- Larger mortgage company packages several loans and resells to another company.*
- New company repackages some of the loans and offers them to an investment company as a mortgage backed security or investment trust.*
- They are then traded on the open market.*
- Investor hires a "loan servicer" to accept loan payments and communicate with the barrower but servicer has little to no authority over property.
- Borrower defaults.
- Servicer processes default/foreclosure for investor but still has no authority over property.
- During the foreclosure process the home is abandoned, deteriorates and becomes a nuisance.
- Code enforcement pulls the title records from the county but the Deed of Trust lists the original mortgage broker as the beneficiary.
- Code officer calls the mortgage broker, who advises the loan was sold to another company months or years ago and has no interest in the property OR the mortgage broker is no longer in business and there is no answer.
- The Notice of Default lists the servicer.
- Code officer calls the servicer, they advise they are "just the servicer" and have no authority over the property and will not provide current beneficiary info.
- Contact is attempted with the subsequent lenders/investors if known but without their internal tracking #'s they can't locate the property in their records.
- Property sits in limbo, abandoned with no maintenance or security for 4-12 months until the current beneficiary of the Deed of Trust realizes they own the asset.

* New lender/investor should record their interest with the county or MERS

For more information on the MERS (Mortgage Electronic Registration System) go to the following link www.mersinc.org or go directly to the servicer identification page at https://www.mers-servicerid.org/sis/

Attachment "D"
List of Interested Cities

California Cities
Alameda- American Canyon-Anaheim-Antioch-Apple- Valley-Arcadia-Azusa-Bakersfield-Baldwin Park-Banning-Beaumont-Bellflower-Belmont-Big Bear Lake-Brentwood-Buena Park-Cathedral City-Canyon Lake-Chico-Chino-Chino Hills-Claremont-Colton-Compton-Costa Mesa-Davis-Desert Hot Springs -Downey-Dublin-El Cajon-Elk Grove-Emeryville-Escondido-Folsom-Fontana-Fremont-Fresno-Garden Grove-Hayward-Hemet-Hollister-Huntington Beach-Imperial -Indio-La Palma-Laguna Hills-Lake Ellsinore-Lancaster-Lincoln-Livermore-Los Angeles-Milpitas-Modesto-Monrovia-Moreno Valley-Montclair-Murrieta-Napa-National City-Norwalk-Oakland-Ontario-Oxnard-Palm Desert-Palm Springs-Paramount-Perris-Pittsburg-Pomona-Rancho Cucamonga- Rancho Mirage-Red Bluff-Redlands-Redwood City-Rialto-Riverside-Rocklin-Roseville-San Bruno-San Jacinto-San Juan Capistrano-San Leandro-San Fernando-San Mateo-San Marcos-San Pablo-Santa Ana-Santa Monica-Santa Rose-Santee-Seaside-Stanton-Stockton-Southgate-Suisun City-Temecula-Tracy-Tulare-Union City-Upland-Vacaville-Vallejo-Victorville-Vista-West Covina- West Hollywood

California Counties
Amador CO-Butte CO-Orange CO-Placer CO-Sacramento CO-San Bernardino CO-San Diego CO-Riverside CO

Other Interested Jurisdictions
AZ Avondale-Chandler-Mesa CO Longmont FL Clearwater-Coral Gables-Miami–Dade GA Duluth IL Aurora-Chicago-Kanakakee-Round Lake-University Park-Waukegan-Warrenville-Zion-Villages of Addison-Bannockburn- Bolingbrook-Cary-Carol Stream-Carpentersville-Downers Grove-Glendale Heights-Highland Park-Hillside-Lake Bluff-Lombard-Matteson-Oak Park-Orland Hills-Oswego-Park Forest-Palitine-Petone-Plainfield-River Forest-Romeroville-Roselle-Skokie-Suger Grove-Tinley Park-West Dundee-Wood Dale IN Vincennes-South Bend KY Louisville MA Boston-Lawrence-Springfield-Rochester MO Lees Summit NJ Voorhees NY New York NV Las Vegas-Nevada County-Reno OH Clayton-Dayton-Lakewood RI Westerly TN Memphis TX Dallas-Garland WI Kenosha-Milwaukee

US HUD – VA Washington DC

Mr. KUCINICH. Mr. Baker, thank you.

STATEMENT OF DEAN BAKER

Mr. BAKER. Thank you, Chairman Kucinich. I appreciate the opportunity to address the committee.

I'm going to take a little different attack than I think most of the other witnesses have in the sense that what I want to talk about is a concrete measure that I think would directly affect the amount of foreclosures and number of foreclosures we're seeing by simply changing the rules on foreclosure. And the essence of this is—actually I call this an own-to-rent concept that we give people facing foreclosure the option to stay in their home as a long-term tenant. And a version of this was actually introduced just today by Representative Grijalva in the form of a Saving Family Homes Act of 2008. And I would argue that this is, in effect, the most effective way available to Congress to stem the looming foreclosure crisis.

The basic concept is very simple. We simply put in a clause that at least temporarily changes the foreclosure laws so that we set a date, I believe in the law it's July of last year, July 2007, that mortgages issued prior to July 2007, if they go into foreclosure, the homeowner would have the option to stay in their home as a tenant paying the fair market rent. And this would be very carefully targeted. It would only apply to occupants of homes that sold for less than the median price in the area at the time the home was purchased, and it also only applied to owner-occupied homes.

And one of the nice aspects of this is that owner-occupied clause, we know this is frequently exploited. Very often people are not always honest in claiming that they are owner/occupants. In this case that really will not do you any good. You are only going to benefit if you actually are, in fact, an owner/occupant, otherwise the right to stay there as a tenant is not really worth anything. So in that sense it's a very nicely targeted measure.

The other aspects of it, it requires an appraisal of the fair market rent. This also is easily done. We have a well-developed appraisal system. For sale prices you would simply do the same determining what the market rent for a house would be, and that would in turn be adjusted by the Consumer Price Index, which is readily available each year from the Bureau of Labor Statistics.

It also has a very nice feature. It requires no tax dollars. We don't have to go running around trying to take money from programs for low-income tenants. It requires no tax dollars; it doesn't require any government money to fund it. It requires no new bureaucracy. Everything is already in place. It's simply part of the foreclosure structure. We don't have to set up a new bureaucracy. And that also means that it can be implemented without delay. We don't have to put this in place and then wait for 3 months, 6 months to make sure that we have the administrative apparatus to deal with it. As soon as Congress were to pass the law, it could immediately take effect.

Now, the benefits, I think, are very direct and very clear. First and foremost, obviously it assures housing security, that in the event you have a homeowner that likes their home, they like the schools, they like the neighborhood, they have the option to stay there as a tenant. It also means that the house doesn't go vacant,

obviously, if they're staying there, so we don't have the problem of vacant property being stripped, being vandalized, being used as a crack house, etc., the issues that have already being raised. We don't have that problem.

Also, and I think this is very important, perhaps the most important part of it, is I actually think it will secure home ownership, because the point here is you make foreclosure a much less attractive option for the lender. They can't simply throw the person out on the street. They're stuck with the tenant for a very long period of time. Recognizing that this is a much less attractive option, the lender is far more likely to sit down and try to negotiate terms with the homeowner that will keep them in the house as a homeowner, which I think is everyone's first best solution. And this in effect puts some muscle behind the exhortations that President Bush and others have made urging lenders to do just that. So I argue that in many ways this would accomplish exactly what we want as a very well-targeted and costly measure.

Let me answer one objection, because I've discussed this with many economists, and the objection that most often has been raised—and I'll mention one economist in particular that raised it a few weeks ago when we were testifying together. Larry Summers, the former Treasury Secretary, complained that he thought it was good, this would be the best way to keep people in their home, but he objected because he felt this would interfere with the sanctity of contract.

And what I would just say on that is that I view the sanctity of contract also as being very important, but I will note that there are certainly times where Congress has felt it was appropriate to override concerns about sanctity of contract. And the most obvious case that I can mention in the recent past was that when they recently changed the bankruptcy law, they chose to apply that retroactively to debt that was incurred under preexisting bankruptcy law. So in that particular case, in the case where we changed the law in a way that was adverse to debtors, Congress apparently was not concerned about the sanctity of contract. So I would say that need not be, you know, an overriding concern; an important concern, but need not be an overriding concern.

Last, just in commenting on this, I have talked about this around Washington and around the country a fair bit, and I point out that this is actually an idea that has attracted a lot of bipartisan support. Some of the strongest proponents are actually fairly conservative Republicans. I will mention Desmond Lachman, who is a fellow at the American Enterprise Institute, who has been a very strong proponent of this proposal. Another person of some prominence, Andrew Samwick, who was a top economist in President Bush's administration, again was a very strong proponent. We, in fact, coauthored a column on it advocating this sort of solution.

So just to sum up, I think that in principle we can do something here that offers us a very quick, very costless, very bureaucracy-free way of dealing with the most immediate and worst effects of this problem.

So I'll conclude my testimony. I just do want to add I would very much welcome the opportunity to address the question you raised

with other witnesses about moral hazard. I think that's an interesting—some things you may find interesting on that topic.

Mr. KUCINICH. Thank you very much, Dr. Baker.

[The prepared statement of Mr. Baker follows:]

Testimony of Dean Baker

Before the Domestic Policy Subcommittee of House of Representatives Oversight and Government Reform Committee Hearing on Policies to Mitigate the Foreclosure Crisis

May 21, 2008

Thank you, Chairman Kucinich, for inviting me to share my views on the mortgage crisis with the subcommittee. My name is Dean Baker and I am the co-director of the Center for Economic and Policy Research. I am an economist, and have been writing about the housing bubble since 2002.

The current situation in the housing market is potentially the largest economic crisis in the post-World War II era both for the country as a whole, and the millions of homeowners facing the loss of their home. By its actions, Congress can help to either ameliorate some of its worst effects, or exacerbate the problems. For this reason, it is crucial that it consider carefully the implications of any legislation.

I would like to present to the subcommittee my "Subprime Borrower Protection Plan," the main thrust of which is temporarily alter the foreclosure process in recognition of the unusual circumstances facing the housing market. The plan would allow low and moderate-income homeowners facing foreclosure the option to remain in their homes as renters for a substantial period of time (e.g. 10 years) in which they would pay the fair market rent.

This measure could potentially provide housing security to millions of families facing foreclosure. It does so in a way that requires no taxpayer money and no new bureaucratic structures, and it can begin to have an impact immediately after Congress approves it. This temporary change in foreclosure rules would also give lenders substantial incentive to renegotiate the terms of the mortgage, increasing the likelihood that many families will be able to stay in their homes as owners.

In the rest of my testimony I will outline some of the specifics of the proposal and highlight the aspects that are most important. I also will take a moment to respond to the main objection that has been raised against this proposal – that it would interfere with the sanctity of contract.

The Subprime Borrower Protection Plan

The basic point of the subprime borrower protection plan is to protect homeowners who were victimized by predatory mortgages and the collapse of the housing bubble from being thrown out of their homes. It accomplishes this goal by temporarily changing the rules on foreclosure, to gives homeowners facing foreclosure the option of renting their home, for a substantial period of time, at the fair market rate. This rate would be determined by an independent appraiser in the same way that an appraiser determines the market value of a home when a bank issues a mortgage.

The proposal can be structured in such a way to ensure that it is limited to low and moderate income families and that it only applies to those who were caught up in the housing boom and subsequent bust of the last few years. These limitations can by applied by setting a limit on the value of the house to which the act would apply and the dates of the mortgages that would be affected.

For example, the change in rules can be limited to houses that sold for less than the median price at the time in the relevant metropolitan area. Congress could of course opt to extend the benefit more widely by allowing the change in rules to apply to somewhat higher-priced homes, for example 1.2 times the median price, or alternatively narrow the range of beneficiaries by setting the cap at 0.8 times the median price. This price information is readily available from the National Association of Realtors.

The benefit can also be time-limited by setting an end date for the mortgages to which the rule would apply. For example, Congress could restrict this change to mortgages that were issued before July 1, 2007. It can also set a beginning date, although very few older mortgages are ending up in foreclosure, so putting a beginning date would have little impact.

In subsequent years, rents will be adjusted by the Labor Department's consumer price index for rents in the area. If either the owner or renter believes that their rent is unfair, they can arrange, at their own expense, to have the court make a second appraisal.

After the foreclosure, the mortgage holder is free to resell the house, but the buyer is still bound by the commitment to accept the former homeowner as a tenant for the full period granted in the proposal. In effect, they could only remove the tenant through a process establishing just cause, such as non-payment of rent or damage to the property.

The Benefits of the Subprime Protection Plan

The most obvious benefit of the proposal is that it would immediately give millions of low and moderate income homeowners facing foreclosure protection from losing their home. There would be no need to set up any new bureaucracy or administrative structure, the protection is put in place the moment the plan becomes law.

The benefit can also be targeted precisely to the low and moderate income homeowners that there is the greatest public interest in assisting. The cap on the value of the home will ensure that upper income homeowners will not benefit under this plan. Similarly, the nature of the benefit – being allowed to stay in the home as a renter – will ensure that speculators will not benefit, since they have no interest in becoming tenants. (The law should also be written to only apply to owner-occupied housing.)

By keeping homeowners in their homes, this act will prevent the sort of disruptions to the lives of working people and their children which results from being thrown out of their homes through foreclosure. This proposal will also prevent the sort of blight that afflicts neighborhoods with large numbers of foreclosed homes. Under this proposal, homes will stay occupied. Even if the family is not still a homeowner, they will be a tenant with a long-term commitment to the house that they rent.

At least as important as these considerations is the fact that the change in foreclosure rules will provide lenders with a substantial incentive to renegotiate the terms of the mortgage in a way that allows the family to remain in the house as a homeowner. Banks and other mortgage holders do not want to become landlords. If they became landlords as a result of this foreclosure procedure they would almost certainly find it necessary to hire a management company or to sell the home at a price that is substantially lower than what it would command as an unoccupied single family home.

Since most lenders would view these as unattractive options, they are likely to seriously commit themselves to negotiating terms with homeowners that allow them to remain in the house as homeowners. While there will undoubtedly be cases where it not possible to reach such an agreement, it is quite likely that more families will stay in their homes as homeowners as a result of this plan than will end up as renters. For this reason, it should be viewed as a measure that is actually likely to promote continued homeownership, in addition to providing housing security.

The Subprime Borrower Protection Plan and the Sanctity of Contract

One of the main criticisms that has been raised against the subprime borrower protection plan is that it interferes with the sanctity of contract by retroactively changing the terms under which mortgage contracts are enforced. While it is reasonable to be concerned about the sanctity of contract – Congress should be reluctant to interfere with the terms of private contracts – the events that have created the current mortgage crisis are extraordinary. Furthermore, there have been other instances where Congress has shown little concern with the sanctity of contract in structuring legislation, most notably the bankruptcy reform bill that was passed in 2005.

In the bankruptcy reform bill, Congress restructured rules on bankruptcy to make it substantially more difficult for individuals to discharge debt through the bankruptcy process. This bill is relevant to the current situation because Congress applied the change

in bankruptcy rules retroactively. The harsher bankruptcy rules applied not only to new debt incurred after the change in the bankruptcy law, but also to debt that had been incurred prior to the passage of the law under the previous set of bankruptcy rules.

This meant that individuals who borrowed money when one set of bankruptcy rules were in effect, could suddenly be forced to repay their debts under a new set of bankruptcy laws. Congress was apparently willing to ignore the fact that both borrower and creditor presumably set their contractual terms (specifically the interest rate) based in part on the bankruptcy rules in place at the time.

In the case of the subprime borrower protection act, Congress is effectively changing the rules of enforcement for mortgage contracts just as it previously changed the rules for collecting debts more generally when it changed the bankruptcy laws. The main difference is that the subprime borrower protection plan is a change that benefits the borrower instead of the lender.

Conclusion

The collapse of the housing bubble has created a crisis in the nation's housing market unlike any that we have witnessed since the Great Depression. While much of the harm from this crisis became unavoidable once the housing bubble grew to dangerous levels, Congress can seek to mitigate the pain to the most vulnerable segment of the home-owning population.

Temporarily changing the foreclosure rules, to allow homeowners facing foreclosure the option to remain in their homes as renters, will provide housing security to millions of families facing foreclosure. It will also give lenders a real incentive to negotiate terms that allow homeowners to stay in their houses as owners.

This proposal requires no new government bureaucracy, nor any expenditure of tax dollars. Furthermore, it would require no lead time, it can provide protection to homeowners immediately after it is signed into law. For these reasons, I hope that the subcommittee will carefully consider the merits of this proposal.

Mr. KUCINICH. Lets go to questions of the panel. I would like to begin the discussion with Mr. Leeper about property maintenance. Your city is holding the lenders responsible for upkeep of vacant properties. I think people on this subcommittee would be interested to know how does the city of Chula Vista hold Wells Fargo, for example, a $48 billion company, number 41 on the Fortune 500, how do you hold them accountable?

Mr. LEEPER. My father told me that money talks. All mine says is good-bye.

Mr. KUCINICH. There's another part of that equation then.

Mr. LEEPER. That's true. And we don't walk. I have contacts in Wells Fargo now that I can call directly. When we find a property, the hardest part is finding who owns the note now. But once we find that Wells Fargo Home Mortgage holds this note, I have an e-mail address and a direct phone number now to someone in Des Moines, Iowa, where their problem property division is, that has shown such interest that they've actually flown out to Chula Vista to look at our city and see what the impacts are.

Mr. KUCINICH. Do you issue fines to scofflaws?

Mr. LEEPER. Yes, we do.

Mr. KUCINICH. And have you sued to enforce your ordinance?

Mr. LEEPER. We have liened properties. Our liens are going as a special assessment on the property taxes, and they are paid.

Mr. KUCINICH. And are you keeping up with the problem with this ordinance?

Mr. LEEPER. We were initially. It has gone to where I have to add staff now, take them off of other items that are as important, but——

Mr. KUCINICH. Do municipalities need additional funding for code enforcement?

Mr. LEEPER. In a word, yes.

Mr. KUCINICH. This is one of those issues that relates to HUD. And in the past we had a general revenue sharing that cities could then draw from and determine what their needs were and be able to apply money accordingly. But would you agree that if cities are going to be empowered to deal effectively with the effects of the subprime scandal, that housing enforcement is where it begins?

Mr. LEEPER. Yes. Code enforcement is a very——

Mr. KUCINICH. Code enforcement.

Mr. LEEPER. Code enforcement is a very integral cog in the wheel.

Mr. KUCINICH. Mr. Mallach, did you want to get in on that?

Mr. MALLACH. If I could add to that, first I agree 100 percent. I think they do need additional resources, but they also—and I think this is particularly the case in the older cities in the Midwest and the Northeast—they also need significant help building their capacity to do it right, using technology so they can operate efficiently.

Mr. KUCINICH. What capacity needs to be built?

Mr. MALLACH. Well, the skills, the skills of the inspectors; the ability of the code enforcement departments to organize their work so they are not complaint-driven, but systematic; their ability to use the kind of technology that increases their efficiency and gets away from creating mountains of paper that typically get lost.

Mr. KUCINICH. Does the Federal Government have any role in that at all?

Mr. MALLACH. Well, I'll say two things. One, certainly financial help could be done. The other thing, and I know the Federal Government has done this in the past in other areas, is condition other assistance on getting your local house in order, so that you have to have a properly functioning code enforcement and nuisance abatement operation in order, say, to be eligible for property acquisition or demolition money.

Mr. KUCINICH. What about incentives required in dealing with the real estate industry?

Mr. MALLACH. Pardon?

Mr. KUCINICH. What about incentives that may be required in dealing with the real estate industry? Are you concerned about creating a moral hazard, and would you characterize any aspect of what we're talking about as being a bailout?

Mr. MALLACH. I am very concerned about a moral hazard issue there. And I find myself very much torn, because I think unless—and this has to be done, I think, at the national level.

Mr. KUCINICH. Would you define for people who may have just joined us what you mean by "moral hazard?"

Mr. MALLACH. A moral hazard is essentially where you bail out somebody who has misbehaved and thereby give the rest of the universe encouragement to similarly misbehave in anticipation that they, too, will be bailed out.

Mr. KUCINICH. Give us an example.

Mr. MALLACH. Well, again, suppose if—and this is an extreme case—suppose the Federal Government offered to buy out people's—these mortgages that are now under water at 100 cents on the dollar. That would send a message to everybody involved in the financial world that they could conduct their business the way the subprime industry has done so for the past 8 or 10 years, and the Federal Government would bail them out.

Mr. KUCINICH. Thank you.

I want to ask Mr. Baker here before I go to Mr. Tierney, as an economist what would you say to the objection raised by the administration that the bill that Congress just passed, H.R. 5818, creates a moral hazard and constitutes a bailout; what would you say?

Mr. BAKER. I think there can be some issues of moral hazard, but that's going to be true in almost anything the government does, that there's always some issues. I think in this case they're relatively limited.

I would just point out it's ironic that this administration would get upset about the moral hazard in that case, but they've been completely unconcerned about the moral hazard involved in the Federal Reserve Board's recent actions vis-a-vis the investment banks, because this really goes very much to the heart of the housing crisis we're seeing.

What Ben Bernanke, the Chair of the Federal Reserve Board, said is that he's going to come to the aid the investment banks in the sense that he will back them up if they get into trouble. This does two things. On the one hand, it gives the investment banks a free ride in having been very heavily overleveraged. They're paying no price for that. They're shareholders, they're top executives.

They made enormous fortunes from overleveraging themselves, something I think almost everyone agrees on. And Ben Bernanke said that the Fed, the agent of the government, the central bank, is going to hold them harmless.

Second, the investors, we talk about the international investment flows, these people obviously didn't know what they were doing. What the market is supposed to say is, well, then, you lose your shirt. But what Ben Bernanke said is, no, the Federal Government through its central bank is going to come in and guarantee your bad debts.

So that's a huge aspect of moral hazard that's really very much at the center of this problem, because if they didn't mindlessly provide that money, and if the investment banks didn't become so overleveraged, we wouldn't have seen the sort of run-up in housing prices, the sort of explosion of subprime lending. That couldn't have happened. So that's a moral hazard very much at the heart of the story, and to the best of my knowledge, the Bush administration has been very silent on it.

Mr. KUCINICH. Thank you, Mr. Baker.

Mr. Tierney.

Mr. TIERNEY. Thank you.

Just so you will know, people in my district didn't miss that. When I go around to community meetings, they get that right away.

Mr. BAKER. That's good.

Mr. TIERNEY. What about the Bear Stearns clients all got bailed out, and here we are worried about an individual homeowner, and what's the difference on that?

Mr. Baker, I'm interested in your proposal. You mentioned you target only those houses that have a value less than the median price of the market in that area; is that what you said?

Mr. BAKER. That's correct.

Mr. TIERNEY. Explain to me why that is.

Mr. BAKER. Again, this is something obviously in actual passage you would decide who you want to benefit from it. But my idea in tying it to the median home price in the area, and I believe Representative Grijalva stuck to that in his bill, is that you want to help the people who are sort of least able to deal with the problems themselves.

Now, if you envision going to higher-priced homes, we might say that those people bear more responsibility for their own actions. Now, whether the median price is the best place to cut that off, that's, you know, a judgment call. Maybe you would want to have that be higher. But I think at some point—and if we're talking about million-dollars homes, we might sort of bristle at the idea that these people aren't able to take care of themselves.

Mr. TIERNEY. It just seemed a little arbitrary for me, because at some point if somebody is just over the edge, and I didn't know if there was some other rationale for that. I think we may want to look at how we measure that, because certainly some people might pay a little more than median value but still be in just as much trouble in sort of an equivalent fault issue on that. But thank you for the answer on that.

So it seems to me with that sense of a situation where the lender is not getting paid back on their loan, but they foreclosed, they can't get the people out of the house, if they don't foreclosure and the person rents it, their fair market value of the rent may not equal what they were getting on their loan, and how does that not become a confiscation of their property?

Mr. BAKER. Well, it's certainly a loss for the lender. They are going to be taking a loss on the property. And the issue here is, you know, what sort of enforcement mechanisms is the government prepared to make available to the lender? And in this case, again, I would make the analogy to what happened with the reform of the bankruptcy law a few years back, that there you had people who took out debt under one set of bankruptcy rules, which were comparatively lenient, and then the government changed that. And to my knowledge at least—now, maybe there's a court case I'm not familiar with, but to my knowledge at least, that's not been contested at all in court. They said the government was free to change the enforcement rules after the fact.

So there certainly is an aspect here that the lenders will take a loss, because obviously they're not getting their preferred course of enforcement, so they are taking a loss, but they are being compensated. But, you know, again, I'm not a lawyer here.

Mr. TIERNEY. I was going to ask you if you happened to have some lawyers look at that in terms of the constitutional implications of taking on that. If they basically have somebody paying less than their value, there's not really sort of an enforcement mechanism. It's actually you've disallowed them the use of their property and stopped them from enforcing their mortgage to them and giving them less in return.

Mr. BAKER. The lawyers I have spoken to on that, I've spoken to a number of lawyers, in their view they thought it would be upheld in the courts since they are getting compensation. So it's not a question that they are getting nothing. They are getting compensation. They aren't getting as much compensation as they would like, but they are getting compensated.

Mr. TIERNEY. Let me just ask each of the other gentlemen what your thoughts are on that proposal.

Mr. MALLACH. First, I think it's basically a very good idea. And, in fact, I should mention that I've been working with a coalition in New Jersey, and we have recently gotten a bill introduced in both houses of the New Jersey State Legislature which, among other things, would enact a similar provision.

But I think there's one difference, and which I think responds to your issue, which the way it's written under the New Jersey bill—and this hasn't been law yet, clearly—is that the owner would be allowed to remain in the property as a tenant and pay the fair market rent, except if the lender who had taken title to it subsequently sells it to a party who wants to use it for their own domicile, then the owner would be given 60 days notice, which is the requirement under the State antieviction law, and then would be required to vacate in order that the new buyer could move in. So in that case the lender has no loss whatsoever, because at the point when the lender is ready to have the property actually be utilized, the former owner has to vacate. But the principle is still the same.

The owner should be allowed to remain in the property as a tenant as long as they can.

Mr. TIERNEY. Mr. Leeper.

Mr. LEEPER. I've had conversations with some of the folks in the lending industry that are actually, at least in Chula Vista, considering leaving those people in the property, because then it's not vacant and subject to our ordinance, which I'm all for. Occupied properties fall victim to theft and vandalism far fewer, at a lesser rate than unoccupied properties. They're generally more maintained, and they don't become the rotting tooth in the smile of the neighborhood. So anything that they can do to continue to keep the neighborhood as stable as possible, be it an own-to-rent or even leaving good solid renters in, you know, while the property is being marketed to somebody who wants to use that residence as an owner-occupied would be a good thing.

Mr. TIERNEY. Mr. Baker, what do you say to Mr. Mallach in New Jersey's adjustment to your proposal?

Mr. BAKER. Obviously a lot would depend on what's on the table and what's politically feasible, and you're the better one to answer that than me. But I think that would be certainly a very big improvement over current law. Now, it gives less security to the homeowner who is facing foreclosure, so I would prefer something that gives them the option to stay there as a long-term tenant. But certainly that would be much better than the situation as it is now, because in many cases they will be able to stay there for a substantial period of time, and it does certainly address the problem that we won't have the property going vacant, so it does get us much of the way there.

Mr. LEEPER. According to the real estate industry, occupied properties are more marketable as well, so it maintains the value and helps retain the value of the entire neighborhood.

Mr. TIERNEY. Mr. Chairman, I have to leave, but I want to tell you I want to thank you for having this hearing and for the excellent witnesses that you presented, and thank all of them. You really help us think through this issue and bring it down to the neighborhood level where it affects us all. And so thank you for your time. Thank you for your patience in waiting through the votes that unfortunately interrupt us in these afternoon hearings, but I want to congratulate you. And thank you on the hearing, Mr. Chairman.

Mr. KUCINICH. Well, Mr. Tierney, as always your participation helps make a difference in a hearing. Thank you for being here.

Before we wrap this up, I just have one question I want to direct to Mr. Baker. We're talking about moral hazard, and it seems that the administration or the discussion of H.R. 5818 are concerned about the moral hazard of benefiting the so-called actors in maybe bad faith who would somehow benefit from a bill that would make someone not whole, but return someone's financial position. Does the concept of moral hazard seem to apply to Wall Street in this case?

Mr. BAKER. Well, obviously they're not concerned about the aspect of moral hazard applying to Wall Street. You know, again, there has been, I think, fairly explicit on the part of the Federal Reserve Board and Chairman Bernanke an attempt to minimize

the harm that Wall Street has suffered in this crisis, which arguably has some positive aspects to it. I mean, none of us want to see a financial collapse, so arguably that's a positive aspect. But at the same time one could easily talk about putting in place policies that prevent a financial collapse while at the same time extracting some toll on the bad actors.

Mr. KUCINICH. If the buyer is to be aware, is the lender to be prudent?

Mr. BAKER. Absolutely. I mean, that's exactly the point here. The lenders are not being asked to suffer. We've stepped in to prevent the lenders from suffering. And again, if the lenders had acted with good sense, we wouldn't have half the problem we have today.

Mr. KUCINICH. Thank you very much.

I'm Dennis Kucinich, Chairman of the Domestic Policy Subcommittee of Oversight and Government Reform. Today's hearing has been entitled, "Neighborhoods: The Blameless Victims of the Subprime Mortgage Crisis." This has been one of a series of hearings, this subcommittee examining the impact of the subprime mortgage fiasco on the neighborhoods of our Nation. This subcommittee is going to continue to probe this matter deeply, as well as to, as we have had, recommend legislative changes and legislative improvements that will somehow provide some remedy, as some of you have worked out in your respective communities.

I want to thank all of the witnesses for their testimony, for their patience today in what has been a very long hearing. And I want to let you know the subcommittee will continue to be in touch with you and your staff as we continue our work to see the residential vitality restored to many of our communities.

This committee stands adjourned. Thank you.

[Whereupon, at 5:25 p.m., the subcommittee was adjourned.]

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